Community Mortgage Banking Project

February 21, 2010

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

Re: RIN # 3064-AD55

Dear Secretary Feldman:

The Community Mortgage Banking Project (CMBP) welcomes the opportunity to comment on the Advanced Notice of Proposed Rulemaking regarding the treatment by the FDIC, as receiver of an insured depository institution, of financial assets transferred by the institution in connection with a securitization or a participation after March 31, 2010 ("ANPR").

We represent community-based mortgage banking companies engaged in residential lending. Our membership includes subsidiaries or affiliates of community banks, as well as independent, privately owned mortgage-banking companies. All of our members sell the large majority, if not all, of the residential loans they originate. As an industry segment, independent mortgage banking companies originate approximately one-third of all residential mortgages and over half of all FHA-insured loans. As such our members, on behalf of the consumers they serve and themselves, have a keen interest in all federal regulatory proposals that have an effect on the residential mortgage backed securities (RMBS) market.

General Comments

A number of observers have raised the issue of whether it is appropriate for the FDIC to include in this ANPR any conditions or standards that do not relate solely to the legal question of whether a legally sufficient transfer of assets has taken place in a securitization by an insured depository institution. We believe this legal question should drive the determination of whether the assets backing the security are beyond the effective reach of the receiver or conservator in the event of a receivership or conservatorship.

Some of the FDIC's proposals may warrant consideration as part of a broader effort to improve the transparency and quality of securitizations. However, we strongly oppose including provisions dealing with underwriting standards, representations and warranties, loan seasoning and risk retention in regulations intended to address the legal question of whether an effective sale of assets has taken placed in a securitization, thus placing those assets beyond the reach of the receiver/conservator. Simply put, receivership regulations are not the appropriate forum to bootstrap broad securitization market reforms.

Second, we question the timing of these regulations, given the fact that the House of Representatives has passed comprehensive financial reform legislation (HR 4173, The Wall Street Reform and Consumer Protection Act) and the Senate is reported to be taking up a bill in the Banking Committee in the near term, that will have a number of significant provisions dealing with securitization. These provisions, both in HR 4173 and the Senate bill will affect the entire market and all players in the market, not solely depository institutions insured by the FDIC.

Finally, we do not undertake to comment on all the questions raised nor all the issues contained in the ANPR. We have restricted our comments to those questions/issues most germane to our members' interests.

Specific Comments

<u>Question 16:</u> *Should additional detailed disclosures be required for RMBS?*

CMBP is strongly in favor of greater transparency in the RMBS market. We believe that investors can only make informed decisions with sufficient information regarding the types of assets backing the security, including loan terms, underwriting standards, borrower and collateral characteristics and valuations. However we question why the ANPR would restrict detailed disclosures only to RMBS issuances. We believe that increased transparency is good for all asset classes and all issuers of asset-backed securities, not just RMBS. As such, we believe the appropriate venue for addressing securitization disclosures is through rules issued by the SEC under their current authority, as well as in response to any new requirements that may be enacted by Congress.

<u>Question 17:</u> *For RMBS should detailed disclosure of underwriting standards be required?*

As stated above CMBP is strongly in favor of greater transparency in the RMBS market. We believe that more detailed disclosure of underwriting standards set by the RMBS issuer would assist investors in making a more informed investment decision and therefore would favor such a requirement. Again, however, we question why this requirement should be limited to only to RMBS and bank issuers. We urge that enhanced underwriting disclosures be applied to all asset-backed securities and all issuers through a comprehensive SEC rulemaking, and not through this receivership proposal.

<u>Question 24:</u> *Should requirements be imposed so that certain fees in RMBS would only be paid out over a number of years?*

We believe such a requirement is an unwarranted interference with the private market and the ability of parties to freely conduct transactions. The lenders that sell the loans to the issuer, the issuer and the investment bankers they work with are all engaged in the manufacture of a financial asset, which will become the property of the investors who purchase the securities upon issuance. The performance of that financial asset will depend upon a number of factors, including the quality of the loans backing the security, the performance of the economy, employment levels, property values in the various localities where the collateral property is located, and the presence of any third party credit enhancement guarantees.

As long as all this information has been provided to the investors, so they are able to make their own informed decision on whether to invest in the security or not, the manufacturers of the financial asset should not be held liable for the performance of the asset, but rather should be held accountable for the accuracy of the information disclosed to investors. As long as the information disclosed is accurate, then investors, with their purchase, assume the risk of the performance of the asset, which is one of the byproducts of ownership of a financial asset.

<u>Question 28:</u> *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?*

Given the major economic and credit market consequences of mandating "risk retention" for securitization issuers, we do not believe that this is an issue that should be addressed through the current FDIC receivership rulemaking process. If the FDIC forges ahead despite these risks, it is critical that the agency understand these risks, and proceeds cautiously and with concern for the broader capital markets.

The CMBP concurs with the concerns raised by Comptroller of the Currency Dugan in connection with this ANPR. The Comptroller has noted that risk retention is an indirect, and potentially inefficient way of attempting to assure sound underwriting for securitized mortgages. A better alternative, he argues, would be to establish an appropriate underwriting framework by regulation, and stipulate that if the standards were met, there would be an exemption from risk retention requirements.

Requiring the sponsor of a securitization to retain an economic interest in a material portion of credit risk of the financial assets is a blunt tool that should be used in a measured and focused manner. Risk retention should be applied to those assets which:

- by their terms and conditions;
- by the level of documentation;

- by the financial capacity of the borrower; or
- because of the value of the collateral, carry a significantly higher degree of risk.

The concept of risk retention should not be applied across the board and it should not be applied to assets that, because of borrower, collateral or instrument terms and conditions, have been demonstrated to carry a lower degree of risk.

Before the US Congress, with respect to financial reform legislation, CMBP has been advocating the establishment, by regulation, of a Qualified Mortgage that would be exempt from risk retention requirements imposed on issuers. The Qualified Mortgage would:

1. Have more traditional terms and conditions, such as full amortization of principle over the term of the loan, a maximum term of 30 years, either a fixed rate or a variable rate with an extended initial term and appropriate yearly and life of instruments caps on interest adjustments;
2. Feature a cash down payment by the borrower and require additional capital-at-risk from loan-level mortgage insurance for lower down payments
3. Require full documentation of the borrower's income and assets;
4. Be underwritten according to underwriting standards the meet or exceed minimum standards set by the regulators.

Mortgages that do not meet these requirements because of loan instrument or borrower characteristics or because of applicable underwriting standards would be subject to risk retention.

The rationale for the establishment of an exemption from risk retention for Qualified Mortgages is two-fold:

1. Borrowers who follow the rules, who have saved a down payment for their home purchase and are willing to fully document the income they will rely upon to service their mortgage debt and their financial and other assets that will backstop their performance, should not be penalized for the excesses of a marketplace that made unsustainable loans to borrowers that were not financially qualified to fulfill their obligations under those loans.
2. Across the board risk retention will unnecessarily drive up the cost of mortgage credit for all consumers – not just higher risk borrowers -- and will transform every mortgage lender into a mortgage investor or guarantor, with the subsequent consequences of higher capital requirements and reduced ability to meet borrower demands for credit because of their greatly diminished financial efficiency caused by across-the-board risk retention.

We urge the FDIC, if it determines to move forward with a risk retention requirement, to focus risk retention on loan products and practices that carry a high degree of risk. Such rules should further establish a Qualified Mortgage exemption to the retention requirements and to define the Qualified Mortgage along the lines we have suggested above. Empirical data from reliable sources should be used develop the qualified mortgage standards.

Question 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?*

CMBP strongly opposes any seasoning requirement for mortgage loans that can be included in RMBS. The proposed 12 month requirement flies in the face of the purposes of securitization, which is to allow an insured depository to meet the mortgage credit needs of consumers when those needs might exceed the bank's own available liquidity for mortgage loans, or when the volume of those loans might cause the bank to have a concentration of mortgage assets in excess of what it deems prudent.

This 12 month seasoning requirement would be a giant step back to the world of the 1970's and 1960's, when the availability of liquid funds for home mortgage lending depended upon the liquidity and balance sheet considerations of local depository institutions. In an effort to overcome those limitations, RMBS were invented, in order to tap capital markets funds that were seeking fixed income, bond-like investments. RMBS made these capital markets funds that would otherwise not be invested in certificates of deposits, funds available for home loans.

As long as greater transparency is created, so that investors an make fully informed investment decisions concerning RMBS, there is no need for either across-the-board risk retention or artificial loan seasoning loan seasoning requirements.

Question 30: *Would the alternative outlined above, which would require a review of specific representations and warranties after 180 days and the repurchase of any mortgages that violate those representations and warranties, better fulfill the goal of aligning the sponsor's interests toward sound underwriting? What would be the costs and benefits of this alternative?*

Representations and warranties are designed to assure investors that the risk they assume in their investment is non-performance of the loans due to changes in underlying economic circumstances, or the borrower's financial condition, not because the loan failed to meet standards set by the securities issuer. Representations and warranties come into play in the event of a loan default attributable to a material failure to meet the underwriting and documentation standards required by the investor. To require issuers to repurchase performing loans, thus depriving investors of the benefits of the performance and burdening the issuers with a repurchase, would be prohibitively impractical and expensive. Representations and warranties should only come into play if, and only if, the loan fails to perform and a defect is found in the loan with respect to the standards set by the issuer as represented to the investor.

<u>Question 31:</u> *Should all residential mortgage loans in an RMBS be required to comply with all statutory and regulatory standards and guidance in effect at the time of origination? Where such standards and guidance involve subjective standards, how will compliance with the standards and guidance be determined? How should the FDIC treat a situation where a very small portion of the mortgages backing an RMBS do not meet the applicable standards and guidance?*

CMBP believes that it would be reasonable and prudent public policy to require residential mortgage loans in an RMBS to meet all statutory and regulatory standards at the time of origination. Though ordinarily this would be a matter that we believe should be left to investors and issuers to sort out between themselves, the mortgage market turmoil has created a need to provide investors with greater assurances on the quality of the loans backing the RMBS being offered and this requirement would greatly assist that effort.

We do not support inclusion of adherence to regulatory *guidance* in this requirement for two reasons: 1. Guidance is, by its nature, not a requirement, but rather an admonition to insured depositories of practices that the regulators believe are prudent and in conformance with regulatory requirements. Including adherence to regulatory guidance would turn guidance into a requirement. 2. Guidance, again by its nature, is much more subjective than regulatory standards. As such it would make for a difficult and inherently unfair determination as to whether a loan, or set of loans, met regulatory guidance.

Finally, we believe that the question about how to treat an RMBS issuance where a small portion of loans do not meet the regulatory standards and guidance highlights the pitfalls in utilizing regulations to determine whether a true sale has taken place for legal purposes to achieve other regulatory goals concerning the lending practices of insured depositories and the quality of the loan assets they either originate or purchase.

Thank you very much for the opportunity to comment on the ANPR. If you have any questions or would desire any additional information please contact me at 571-357-1036.

Sincerely

Glen S. Corso
Managing Director