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12 CFR Part 43  
Docket ID OCC-2013-0010  
RIN 1557-AD40

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12 CFR Part 244  
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RIN 7100-AD70

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12 CFR Part 1234  
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RIN 3064-AD74

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24 CFR Part 267  
RIN 2501-AD53

Re: Section 941 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Credit Risk Retention Re-Proposed Rules

Ladies and Gentlemen,

Wells Fargo & Company ("Wells Fargo") appreciates the opportunity to provide comments regarding the jointly proposed rule ("Re-Proposal") to revise the originally proposed rule

published in the Federal Register on April 29, 2011 (“Original Proposal”), implementing the requirements of section 15G of the Securities Exchange Act of 1934 (“Exchange Act”) as added by section 941 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Section 941”).

Serving the financial needs of American families and businesses requires a diversity of capital sources, inclusive of banks, non-bank financial companies and capital markets solutions, including a well-functioning securitization market. The economic benefits provided by securitization often lower the cost of credit. Additionally, owing to structural benefits such as isolation of the credit from corporate risk through bankruptcy remote structures, cross-collateralization and diversified asset pools, securitizations provide capital to certain sectors that would otherwise find it unavailable. Securitization is an important source of liquidity for the U.S. economy. To properly function, securitization markets require a balance of regulation and appropriate risk management. Achieving an appropriate balance is a difficult process and Wells Fargo appreciates the significant efforts put forth by the various Federal agencies (the “Agencies”) to draft risk retention rules directed toward aligning the interests of participants in the securitization market while at the same time allowing that market to serve the important role in providing liquidity.

Wells Fargo appreciates the Agencies’ efforts to address the comments received in connection with the Original Proposal and we recognize that the Re-Proposal reflects many of our previously submitted comments. However, Wells Fargo continues to have significant concerns regarding aspects of the Re-Proposal and its potential negative impact on certain critical sectors of the securitization market and the availability of credit. The purpose of our comment letter is to highlight some of our specific concerns and to propose solutions that will allow securitization to continue to be a viable source of liquidity.

Our letter is divided into five main sections. The first three sections of our letter address the Re-Proposal’s impact on the largest asset classes originated by Wells Fargo, which include collateralized loan obligations (“CLO”), residential mortgage backed securities (“RMBS”), and commercial mortgage backed securities (“CMBS”). The fourth section of our letter discusses general comments on the forms of risk retention and issues related to calculating “fair value.” The fifth section of our letter addresses other asset classes not previously discussed, including auto loans, credit cards, resecuritizations and tender option bonds.

In the course of preparing this comment letter Wells Fargo has worked closely with a number of trade organizations in connection with their respective comment letters regarding the Re-Proposal, including the joint letter from the Securities Industry and Financial Markets Association (“SIFMA”), the Financial Services Round Table (“FSR”), the American Bankers Association (“ABA”) and the ABA Securities Association (“ABASA” and together with SIFMA, FSR and ABA, the “SIFMA/FSR/ABA/ABASA”), the CRE Finance Council (“CREFC”), the Loan Syndications and Trading Association (“LSTA”) and The Clearing House. In addition, we

have also worked directly with Ashurst LLP and a majority of the sponsors of Tender Option Bond programs (“TOBs”) on a separate comment letter addressing concerns with the Re-Proposal specifically in the context of TOBs. We generally support each of the letters submitted by these organizations, and in some instances, in lieu of providing separate comments in this letter, we specifically endorse the comment letters filed by these organizations. We are also providing separate comments in this letter to certain specific aspects of the Re-Proposal.

## **I. COLLATERALIZED LOAN OBLIGATIONS AND THE ARRANGER OPTION**

The CLO market performs a vital role in the U.S. economy by providing essential financing to borrowers through syndicated institutional term loans (“TLBs”). Companies representing every industry and geographic business sector have aggregate outstanding borrowings of \$640 billion through the TLB market, which receives approximately 58.5% of its funding through CLOs.<sup>1</sup> Borrowers utilize the TLB market to access debt financing at a lower cost of capital than otherwise available, if available at all. The capital provided by this market is vital in order for these companies to execute their business plans. Without a robust CLO market a very significant portion of this TLB capital would not be available and will threaten many sectors of the U.S. economy with real repercussions, including a stagnation of job growth.

The CLO market is also a safe and well performing market for institutional investors, including pension funds, U.S. and foreign financial institutions and insurance companies, with returns that are not easily duplicated by other products. Due to the size and credit characteristics of the average TLB, TLB facilities are typically originated by large regulated financial institutions, such as Wells Fargo, who have the ability to broadly syndicate the exposure to other institutions and significantly to CLOs (these TLB originators are referred to as lead arrangers<sup>2</sup> in the Re-Proposal). With TLBs as collateral, approximately \$265 billion of CLO securities are currently held by institutional investors desiring to gain diverse exposure to the TLB market. Although a CLO may have a total asset value of \$300 million, its assets are comprised of multiple TLB assets of approximately \$1 to \$5 million of a particular TLB, providing investors important credit enhancements such as the benefit of significant diversification within each CLO portfolio and cross-collateralization among its assets.

The TLB and CLO markets are safe well-performing markets in large part because TLB assets are subject to substantial due diligence, both at origination by arrangers and upon selection for the CLO by CLO managers. Borrowers who access the TLB market generally have complex

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<sup>1</sup> S&P/LCD; MarketIt Partners

<sup>2</sup> For the purposes of this letter, we have assumed that in the Re-Proposal, the Agencies used the term lead arranger generically to describe each of the roles which a large regulated entity such as Wells Fargo may be engaged with respect to the origination of a TLB tranche, including our subsidiary national banking association, Wells Fargo Bank, National Association as an administrative agent and the lender required to hold the risk retention portion of the CLO-Eligible tranche, and as our subsidiary registered broker dealer, Wells Fargo Securities, LLC as a lead arranger.

capital structures. Accordingly, Wells Fargo and other financial institutions arranging the TLB facilities typically have multi-faceted and dynamic relationships with these customers. These relationships often include more standard commercial bank products, such as revolvers, derivatives and treasury management services, as well as capital markets products such as high yield and equity securities distribution. These relationships require the arrangers to continually evaluate their customers' economic and management performance, as well as macro and micro economic factors specific to the borrower, industry or geographic sectors and the economy as a whole. Wells Fargo applies a similar level of analyses and care when acting as lead arranger on behalf of a broader syndication. Importantly, our underwriting policies and procedures are governed in part by the recently revised Interagency Guidance for Leveraged Lending issued by the FRB, the FDIC and the OCC on March 22, 2013. This guidance specifically contains underwriting and risk management standards for leveraged lending, including TLB tranches, which are designed to ensure financial institutions lend to creditworthy borrowers in a safe and sound manner.

In addition, managers of open market CLOs employ seasoned portfolio management and credit analysis teams that perform independent due diligence on each TLB prior to purchase and on an ongoing basis, ensuring that each loan meets the collateral requirements of the CLO. Importantly, throughout the financial crisis there were virtually no principal losses to CLO investors at maturity.

Wells Fargo appreciates that the Agencies spent a considerable amount of time reviewing and addressing the numerous comments made regarding CLOs with respect to the Original Proposal. While we understand that the Agencies disagree with some of those comments, we continue to maintain our position that Section 941 does not require the Agencies to impose a risk retention obligation on managers of CLOs, because they are not "securitizers" within the meaning of Section 941. Therefore, we respectfully request that the Agencies reconsider their position articulated in the Re-Proposal and not require the CLO managers to retain risk pursuant to Section 941. In the alternative, we respectfully request that the Agencies exercise their authority under Section 941(e) to establish an exemption from the risk retention requirements for open market CLOs. The Agencies correctly acknowledge that, for most managers of CLOs, holding the risk retention piece is financially prohibitive. Therefore, this potential solution to a risk retention requirement is not viable.

Unfortunately, the alternative option ("Arranger Option") outlined in the Re-Proposal to have the arranger satisfy the risk retention obligations of Section 941 is also not viable. The Arranger Option is not appropriate for banks and other highly regulated financial entities such as Wells Fargo under current regulatory guidance, and such regulated entities represent almost the entire market of originators of the type of loans that comprise the assets of a CLO. As discussed above, Wells Fargo's relationships with TLB borrowers is multi-faceted, complex and dynamic, and, in almost every instance, includes credit exposure in one or more forms. We continually evaluate the borrower and, when required, adjust our credit exposure and support to them. The

requirement that arrangers such as Wells Fargo hold additional exposure to a borrower, in the form of a risk retention interest which is unhedged and held to maturity without consideration of the credit quality of the borrower or other economic factors, is generally inconsistent with prudent lending practices and discouraged by our internal lending policies which are derived in part in response to regulatory safety and soundness requirements related to this type of exposure. Further, requiring us to retain the TLB risk retention piece would introduce aggregation concerns and impact the amount of other traditional banking products we can extend to such borrowers as well as to other borrowers in similar industry and/or geographic sectors.

Virtually the entire TLB market today is arranged by regulated financial institutions like Wells Fargo. Only a handful of non-regulated entities have a balance sheet of sufficient size to arrange, distribute and satisfy the proposed arranger risk retention requirements for TLBs, which is nowhere near the number of entities that would be required to supply the level of capital necessary to satisfy this critical need for liquidity. Assuming the Arranger Option suggested by the Re-Proposal were put into effect, as neither regulated nor unregulated arrangers would be able to generate enough CLO-eligible TLBs, the TLB and CLO markets would experience a severe contraction resulting in a significant reduction in liquidity to a critical sector of the U.S. economy.

As a member of the LSTA, The Clearing House and the Structured Finance Industry Group (“SFIG”), Wells Fargo is actively developing proposed alternative solutions to the CLO risk retention requirements which seek to preserve the robust, efficient and critical commercial loan, TLB and CLO markets, thereby supporting U.S. borrowers and the U.S. economy, while at the same time satisfying the risk retention requirements of Section 941. In that respect, notwithstanding our position that Section 941 does not require the Agencies to impose a risk retention obligation on managers of CLOs, Wells Fargo fully supports the recommendations and proposals put forth in the comment letters submitted by the LSTA, The Clearing House, and SFIG. Given the short amount of time that we have had to review this Re-Proposal, we will continue to consider alternatives internally and with the industry groups indicated above. To the extent that our view changes or differs from those set forth in the industry comment letters referenced above, we will provide additional comments in a supplementary submission.

## **II. RESIDENTIAL MORTGAGE-BACKED SECURITIES**

Wells Fargo supports many of the revisions made by the Agencies in the Re-Proposal relating to RMBS. Overall, we believe that the Re-Proposal is a positive step from the previous set of risk retention proposals and should assist market participants in redeveloping a healthy and sustainable RMBS market. However, we still have substantial concerns with respect to several sections of the Re-Proposal as it relates to RMBS.

### **A. Exemption for Qualified Residential Mortgages**

#### Qualified Residential Mortgage Definition

The Re-Proposal defines a QRM as equivalent to a QM as defined in section 129 C of the Truth in Lending Act (“TILA”) and the regulations issued thereunder by the Consumer Financial Protection Bureau (“CFPB”). Wells Fargo strongly supports alignment of the definitions of QRM and QM in the Re-Proposal. We believe this approach will provide responsible risk protections for investors, as well as support the broad availability of affordable mortgage credit to consumers.

The goal of QM is to support the origination of sustainable mortgage loans without risky features and for which the consumer’s ability to repay has been determined. Now that the CFPB’s QM regulation has been published in final form, to be effective January 10, 2014, we believe QM will support production of quality loans that are also deserving of the exemption from risk retention. There are various key elements of the CFPB’s QM rule that represent sound underwriting approaches that should result in the production of loans with prudent risk profiles. Some of these elements are: the inclusion of the maximum 43% debt-to-income (“DTI”) ratio and specific DTI calculation standards in the “standard” definition of QM; the inclusion of the temporary special rule (“TSR”) allowing for certain GSE and agency-eligible loans to qualify as QMs for certain limited periods, including while the GSEs are in conservatorship; and the recently published FHA QM proposal.

In addition, aligning the QRM definition to QM will greatly simplify compliance for both lenders and sponsors, which should avoid introduction of significant additional costs into both the origination and secondary market processes, while also supporting the continued affordability of credit.

Assuming that the final risk retention rule aligns QRM and QM, the Agencies will need to ensure that QRM in fact aligns with QM in all respects. First, the Re-Proposal states that the definition of QRM encompasses all forms of QM, as defined in section 129 C of TILA. Section 129 C of TILA encompasses not only the definition of QM under the “standard” definition and the TSR for GSEs, promulgated by the CFPB, but it also includes the successor rules to the TSR for other agency-eligible loans such as the now-proposed FHA definition. As a result, the Agencies should be clear that all QM definitions under section 129 C are covered by QRM. In addition, the final risk retention rule should specifically reference that the QRM definition is intended to incorporate all regulations and other guidance adopted by the regulators responsible for the maintenance of the respective QM definitions. This can be accomplished by including the italicized language below in the definition of QRM:

§ \_\_\_\_ .13 Exemption for qualified residential mortgages.

(a) Definitions. For purposes of this section, the following definitions shall apply:

Qualified residential mortgage means a “qualified mortgage” as defined in section 129 C of the Truth in Lending Act (15 U.S.C.1639c) and regulations issued thereunder. *Upon the effective date of any revision to the definition or rules relating to QM by the CFPB or*

*any other federal agency designated under Section 129C(b)(3)(B(ii) to promulgate a separate definition of QM, the QRM definition under the then current risk retention rules shall automatically be revised to conform such revised QM standards on the same effective date.*

Second, the Agencies should explicitly state that there is full alignment of QRM and QM throughout the life cycle of a loan. In other words, in addition to aligning the process for determining that a loan is a QM, including all documentation and underwriting requirements, the process for any subsequent determination that a loan is not a QM, including the impact of a repurchase, must also be in full alignment with the QRM requirement. This is necessary to avoid confusion and inconsistency in the primary and secondary markets, as well as to obtain efficiencies in the areas of origination, sale, and servicing. Finally, to the extent that any changes are made to the QM definitions maintained by the CFPB or FHA, VA, RHS, or USDA, these changes would need to become part of the QRM definition.

#### Additional Risk Retention Exemption Requirements

##### *Loans must be performing as of the closing date*

In addition to the stipulation that all loans are QRM loans, in order to qualify for the exemption from risk retention, all of the loans in the securitization pool must be performing as of the closing date of the securitization. While we support the Agencies' requirement that all of the loans must be performing, we believe that measuring performance data as of the closing date, as opposed to the cut-off date, is unworkable. Therefore, we suggest that the Agencies revise the requirement so that all loans must be performing as of the cut-off date.

For RMBS transactions, the pool data (including any delinquencies) are finalized as of the cut-off date. This is necessary so that sponsors, underwriters and accountants have adequate time to perform the multitude of calculations that are required for the offering documents. This includes calculating and confirming the number and principal balances of the underlying mortgage loans, as well as certain other statistical information, such as the geographic concentrations, interest rate averages, FICO averages, LTV ratios, DTI ratios, etc. Transactions are generally priced with investors after delivery of the preliminary offering document. Pricing information is then added to the collateral information for the final offering document. Only after all of these calculations, checks, etc. have occurred will the transaction close.

If any loans become delinquent between the cut-off date and the closing date, the Re-Proposal would require the sponsor and underwriters to produce new statistical information with respect to the entire collateral pool, which may require a new preliminary offering document and, potentially, a re-pricing of the transaction. This process may even have to be repeated if more loans become delinquent prior to the new closing date. While in theory QRM loans should not experience significant delinquencies, the proposed definition of delinquency as only 30-days past due is a very tight standard and it is possible that one or more delinquencies will occur between

the cut-off and closing date. It should also be noted that under existing securities laws, if the sponsor obtains knowledge between those dates that a material portion of the loans are delinquent (or there are other characteristics of the loans that are materially inconsistent with the disclosure in the offering documents), the sponsor would revise its offering document and re-price the transaction.

Our primary concern is that by setting the delinquency measurement as of the closing date there could never be certainty around pricing and closing dates. This would create an extremely challenging market environment for RMBS transactions. Therefore, we strongly urge the Agencies to make the performance measurement date consistent with the market practice of finalizing collateral information as of the cut-off date.

#### *Depositor Certification*

The final requirement for exemption from risk retention is that the Depositor certifies “that it has evaluated the effectiveness of its internal supervisory controls with respect to the process for ensuring that all assets that collateralize the asset-backed security are qualified residential mortgages or servicing assets and has concluded that its internal supervisory controls are effective.” We believe that the Agencies’ desire was to specifically require Depositors to perform an assessment of their internal controls and processes for confirming that loans they represent to be QRM loans are, in fact, QRM loans. We support the Agencies’ goals in this respect; however, we believe that there are more effective ways of accomplishing this objective.

We strongly disagree that any such certification should be delivered directly to investors. We think that a better approach is a requirement that the certification be delivered to the Agencies. Providing a Depositor’s certification to investors could create a more disruptive and expensive RMBS market, and will do nothing to further the purposes of Section 941. Delivering the certificate directly to investors could lead to the filing of unnecessary legal actions since investors may inappropriately read the certificate as an absolute guaranty that all of the loans in the pool are QRM loans and they may be tempted to bring a suit whenever a non-QRM loan is found in a pool. It is also not clear what standard of liability would apply to the certificate if it were provided to investors. Investors already have substantial avenues of recourse under both the securities laws for information provided in the offering documents and under the transaction documents for breaches of representations and warranties. The offering documents will disclose whether or not all of the loans are QRM loans, and provide a description of the sponsor’s origination practices. Additionally, the mortgage loan sale documents will most likely include a direct representation from the seller that all of the loans are QRM loans.

Furthermore, current market practices demand robust due diligence reviews of collateral pools by independent third-party due diligence firms, and demand extensive disclosure with respect to the findings of such third-party due diligence providers. Similarly, in publicly registered transactions, Commission Rule 193 of the Exchange Act requires issuers or underwriters to perform a review of the pool assets designed to provide “reasonable assurance” that the



disclosure in the prospectus regarding the assets (which would include their QRM status) is accurate in all material respects. Regulation AB Item 1111 also requires disclosure of the nature of the review conducted in accordance with Rule 193.

Robust due diligence practices coupled with extensive disclosure and current federal securities regulations are adequate to provide investors with relevant information with respect to a Depositor's process and controls for meeting the requirement that all loans are QRM loans. Therefore, we urge that the final risk retention rules not require that the certification be delivered to investors, but rather, require that the certification only be delivered to the Agencies.

We also urge the Agencies to revise the text of the certificate. The use of the word "ensure" in the proposed certificate creates a threshold concern, as it may be read as a guaranty by the Depositor that there are no non-QRM loans in the pool. However, by requiring that non-QRM loans be repurchased from transactions if they are found to be present, the Re-Proposal itself acknowledges that non-QRM loans may inadvertently be included in a pool, which seems to indicate an internal inconsistency within the Re-Proposal. We believe that the purpose of the certification is to require that Depositors perform a thorough process and compliance review, and as such, the certificate should be revised to clarify that it is addressing the Depositor's internal process as opposed to the ultimate result. To address this problem, the certification could be revised as follows: "Depositor currently has in place internal supervisory controls with respect to the process for meeting the requirement that all assets that collateralize the asset-backed securities are qualified residential mortgages or servicing assets."

## **B. Sunset of Risk Retention**

As we stated in our letter relating to the Original Proposal, we generally agree with risk retention as a tool to better align the interests of sponsors and investors; nonetheless, the benefits of risk retention diminish after a certain period of time. We believe that the Agencies considered this when they provided for the expiration of the transfer and hedging restrictions in the Re-Proposal. However, the required holding period is still too long and should be reduced to 36 months following the closing of the securitization.

The primary purpose of risk retention is to require sound underwriting and, thereby, reduce the likelihood that sponsors securitize low-quality assets and pass the credit risk of those assets along to investors, who are in a worse position to judge loan quality. However, following the closing of a mortgage loan, loan performance data provide third-parties with the information necessary to better understand the quality of a mortgage loan.

Recently, FHFA limited the potential repurchase obligations to 36-months after certain loans are sold to Freddie Mac or Fannie Mae, indicating that an acceptable borrower payment history during this 36 month period would demonstrate the borrower's ability to repay its loan obligation. Similarly, the CFPB has created more flexible QM underwriting provisions for small

creditors who are portfolio lenders, with the condition that the small creditor must hold the loan for a period of 36 months following origination.

While both the FHFA and the CFPB are evaluating the performance of individual loans as opposed to an aggregation of a large pool of loans, we believe the FHFA and CFPB guidance evidences a view that there is meaningful loan performance information after 36 months. Similarly, we believe that 36 months following the closing of a securitization, investor and other third-parties will have loan pool performance information that will allow them to better evaluate the quality of the loans in a particular securitization. Therefore, we believe that the objectives of risk retention are largely accomplished after a 36 month holding period and the prohibition against the transfer or hedging of risk retention should expire after this time.

### **C. Seasoned Loans**

The Re-Proposal has a general exemption from risk retention for all seasoned loans meeting two basic criteria: (1) the loans may not have been modified since origination and (2) none of the loans have been delinquent for 30 days or more. We believe that these criteria are too restrictive and will lead to a reduction in the availability of credit and could have other adverse impacts on borrowers.

#### Loan Modifications

By not allowing loans that have been modified to qualify as seasoned loans, the Re-Proposal will likely have the unintended and undesirable consequence of discouraging lenders from providing borrowers with certain discretionary modifications, which may be both useful and critical. Loan modifications following a delinquency will already be prohibited from the seasoned loan exemption due to the second prong of the requirement relating to delinquencies. However, there are numerous other reasons why a borrower may receive a loan modification that are unrelated to previous borrower payment difficulties. We are unclear as to why the Agencies would want to exclude such modified loans from the seasoned loan exemption.

One premise behind allowing an exemption from risk retention for seasoned loans is that such loans will have performance data and, as stated above, such performance data will give investors a better understanding of the quality of the underwriting. Naturally, modifications change the original underwriting of a loan so that historical performance data may become less reliable. However, new performance data on a modified loan will become available with time. Therefore, the exemption should not include an absolute prohibition relating to loan modifications. Rather, it should allow such loans to qualify for the exemption after a certain period of time following any modification. Consistent with the immediately preceding section of this letter, we believe that 36 months following a loan modification is an adequate period of time for new performance data to demonstrate the quality of the underwriting of the modified loan.

#### 30-day Delinquencies

The Re-Proposal's exclusion from the seasoned loan exemption of loans that have been delinquent for 30 days or more is too rigid and may exclude a number of high-quality loans. Some 30 day delinquencies may be unrelated to the quality of the loan or the borrower. A borrower may take an extended vacation, suffer from a temporary illness or simply have an occasional oversight that causes them to make a single late payment. It seems draconian to exclude loans with such circumstances from the seasoned loan exemption and, therefore, we suggest that the Agencies amend the prohibition to loans 60 days delinquent versus 30-days delinquent.

However, similar to the loan modification requirement, loans that are even 60-days delinquent should not be permanently disqualified from being included in securitizations that are exempt from risk retention. High quality borrowers may still encounter serious difficulties from time-to-time due to circumstances unrelated to their credit quality or the quality of their loan. For example, a borrower may experience a temporary loss of employment or suffer from an illness that adversely impacts that borrower's ability to make his or her required mortgage payments. Although such borrowers may experience brief financial troubles, they may then be able to improve their situation, whether through finding a new job, recovering from their illness or otherwise. As discussed above, a new seasoning period should begin once such borrowers become current on their loan, and we believe that the same 36 month period is appropriate to re-establish the credit quality of the asset.

#### RMBS Seasoning Period

Applicable to RMBS only, the Re-Proposal has an additional seasoning requirement that basically requires a 7 year seasoning period.<sup>3</sup> The length of this seasoning period is too long. Consistent with our reasoning above in Sunset of Risk Retention, we believe that a 36 month seasoning period is sufficient to provide investors with enough payment history to demonstrate a borrower's ability to repay its loan obligation and is consistent with other related regulations. After such 36 month period, a loan has enough meaningful performance data so that it no longer requires risk retention as a means to demonstrate the quality of its underwriting.

### **III. Commercial Mortgage-Backed Securities**

Wells Fargo is the largest commercial real estate loan originator in the United States and a significant investor in CMBS product. As well, through its broker-dealer subsidiary, Wells Fargo has a significant CMBS distribution capability and has regular discussions with subordinate or "B-piece" buyers as well as senior investors regarding all aspects of the CMBS market. With such a broad reach in the CMBS market, we are uniquely positioned to evaluate the potential effect of the Re-Proposal on the CMBS market. The CMBS market has demonstrated strong performance and considerable growth since its inception. The CMBS

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<sup>3</sup> This requirement is essentially 7 years for RMBS because 30-year mortgages are rarely paid down to 25% of their principal balance in their first five-years.

market continues to improve its existing strong disclosure practices and industry standards regarding such disclosure. Wells Fargo recognizes that the Agencies understand some of the unique characteristics of the CMBS market and appreciates the Agencies' efforts to provide specifically tailored options to address those characteristics in the Re-Proposal. We do believe, however, that certain changes are necessary in order to address the concerns behind the Re-Proposal without negatively impacting the availability of credit in a critical and otherwise well performing market.

Wells Fargo is an active member of CREFC and fully supports and endorses the recommendations and comments put forth in the comment letter submitted by CREFC as well as the letter submitted by SIFMA/FSR/ABA/ABASA. These trade organizations serve the constituents of the CMBS market (among others) and their recommendations and comments to the Re-Proposal, when properly considered and implemented by the Agencies, will help to shape a thriving CMBS market going forward. While Wells Fargo is a member of SFIG and supports the advocacy submitted by that group in context of other asset classes as cited in this letter, Wells Fargo has a strong view that SFIG does not have a sufficient market presence reflected in its membership to be expressing either a market view for the CMBS industry or even with respect to a given class of stakeholders within the CMBS industry. Specifically, as described in SFIG's submission, the investment grade investor views ascribed in the SFIG letter that are contrary to our own and the proposals put forth by CREFC represent only a portion of a total SFIG CMBS investment grade investor population of 10 individuals. CREFC cites an investment grade investor forum membership of 61 organizations (with over 100 individual members) and describes in their letter a robust process for discerning the view of that group as well as of the other CMBS market constituencies. Accordingly, Wells Fargo respectfully suggests that the Agencies consider the CREFC position and not the SFIG views.

In order to avoid extensive redundancies in the Agencies' review of the many comment letters they will undoubtedly receive in response to the Re-Proposal, as in other subject matter areas, Wells Fargo is electing to cite its support for the positions of CREFC and SIFMA/FSR/ABA/ABASA and limit our own comments to a few specific points.

#### **A. Single Borrower/Single Credit CMBS**

As the largest commercial real estate loan originator and a significant distributor of CMBS, Wells Fargo is uniquely positioned to evaluate the performance of the different types of CMBS transactions. In particular, we note that with respect to one sub-set of "non-conduit" CMBS transactions that are collateralized by one asset, either a single loan to a single borrower on a single commercial real estate property, a pool of commercial real estate properties included in a single loan to a single borrower or a pool of loans that are cross-collateralized against one another, the performance of these transactions supports an exemption from the risk retention obligations of the Re-Proposal. Our research team has reviewed all CMBS transactions from 1997 through September 2013 and compared single borrower transactions to multi-borrower

transactions. Acknowledging that most single borrower transactions include only the investment grade portion of the loan and treating a loan as delinquent if it has ever become 90+ days delinquent, we determined that single borrower transactions had a cumulative default percentage over that time period of only 3.34%, as compared to a cumulative default percentage for all multi-borrower transactions of 16.12%. Moreover, while the cumulative loss percentage for multi-borrower transactions was 3.06%, the cumulative loss percentage for the single borrower “non-conduit” transactions was only 0.13%. While we appreciate the Agencies’ concerns that fuller asset-level disclosure in offering documents alone is insufficient grounds to satisfy the exemption standards of section 15G of the Exchange Act with respect to “non-conduit” CMBS transactions, this is not the sole rationale for extending the exemption to these types of transactions. We agree with CREFC and SIFMA/FSR/ABA/ABASA that the additional transparency, particularly with respect to single borrower transactions, is an important point to support the recommendation, but we also note the very favorable historical performance data of these transactions identified above and in the CREFC letter. Accordingly, an exemption is also warranted with respect to single-asset or single borrower/single credit CMBS transactions and is important to sustain liquidity in these markets.

#### **B. Qualifying Commercial Real Estate Loans**

While we appreciate the efforts made by the Agencies in revising the definition of qualifying commercial real estate loans (“QCRE Loans”) in the Re-Proposal, we remain concerned that this definition does not go far enough to capture an appropriate universe of commercial real estate loans typically included in CMBS transactions. Accordingly, we urge the Agencies to at least revise the definition of QCRE Loan as proposed by CREFC in its comment letter. These changes include, among other things, allowing for up to 30-year amortization schedules, removing any limits as to loan maturity term, allowing for interest-only loans with an LTV of no greater than 50% and eliminating the lower LTV/CLTV ratio caps for loans documented with appraisals that utilize lower cap rates. These changes are generally consistent with underwriting currently done in the CMBS market and will keep open an avenue into the capital markets for these commercial real estate owners in a way that is consistent with the objectives of the Re-Proposal. It is important to note that even these changes leave the vast majority of high quality commercial real estate loans outside of the current definition of QCRE Loans, requiring that sponsors satisfy the risk retention requirements of the Re-Proposal. Requiring risk retention for such high quality commercial real estate loans will increase the cost of a CMBS transaction and will negatively impact liquidity in the CMBS market and may drive the owners of the highest quality commercial real estate away from the CMBS market, thereby reducing the overall quality of the collateral, a result at odds with the stated intention of the Re-Proposal and Section 941 of the Exchange Act.

#### **C. Multiple B-Piece Buyers**

Finally, we would like to identify one other recommendation made in the response letters from CREFC and SIFMA/FSR/ABA/ABASA that we feel is particularly important to the CMBS marketplace. We are grateful that the Agencies have considered the unique characteristics of the CMBS market by allowing up to two B-piece buyers to acquire the EHRI for a CMBS transaction. However, it is important that these two B-piece buyers be able to hold their interests in a senior/subordinate structure, rather than requiring that they hold their interests *pari passu*. The ability of two B-piece buyers to hold their interests in a senior/subordinate structure will allow the market to appropriately and efficiently price the B-piece commensurate with the risk of loss of each B-piece interest and the risk tolerances of the B-piece buyers. Given that both B-piece buyers will continue to be responsible for due diligence on the entire asset pool and both will be subject to the risk of loss on 100% of their investment, no investor protection will be sacrificed and pricing will be more efficient, thereby reducing the overall cost of capital.

#### **IV. GENERAL COMMENTS**

##### **A. Forms of Risk Retention**

###### Horizontal Risk Retention

We appreciate the Agencies addressing the concerns expressed by many market participants with respect to the premium capture cash reserve account provisions included in the Original Proposal. However, the EHRI option for risk retention as currently proposed does present certain concerns.

###### *Issues related to the Calculation and Disclosure of “Fair Value”*

The Re-Proposal states that, for purposes of calculating a sponsor’s required amount of retention in a transaction, fair value of the ABS interests in the issuing entity must be determined in accordance with GAAP as of the day on which the price of the ABS interests to be sold to third parties is determined. However, the Re-Proposal also requires the fair value of the EHRI to be retained by the sponsor, as well as certain key inputs and assumptions to the calculation, to be disclosed to potential investors a reasonable period of time prior to the sale of any ABS interests.<sup>4</sup> We believe this to be an inconsistency which should be addressed by requiring fair value to be determined after pricing but before closing of the securitization transaction. This would provide an objective and observable measurement for purposes of determining fair value, and may eliminate the necessity of disclosing various inputs and assumptions, certain of which may be proprietary to the calculating institution, inherently subjective in nature and potentially misleading should investors draw impressions or conclusions from the assumptions related to other concepts.

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<sup>4</sup> As discussed below, we do not think that the fair value calculations and disclosures should be required where a sponsor elects to retain risk via retention of an EVI because regardless of whether the sponsor retains 5% of fair value or 5% of face value of each ABS interest, the result would be the same.

Fair value determinations under GAAP are subject to a hierarchy of approaches that often will lead to varying results. Substantial variation is much more likely when fair value is calculated based upon secondary sources or discounted cash flow projections. The most objective approach to calculating fair value would be to base the valuation on an independent observable market price (i.e., the pricing of the ABS transaction)<sup>5</sup>. By requiring fair value to be determined post-pricing but before closing of a securitization transaction, these calculations could be based on the most applicable market-based measurement—the pricing of the ABS transaction. Sponsors could still be required to disclose the expected form of risk retention prior to sale (e.g., eligible vertical interest (“EVI”), EHRI or a combination of both), but the fair value of those interests could be determined shortly after pricing.<sup>6</sup> Aligning fair value calculations with the pricing of the underlying transaction creates an objective measurement for purposes of calculating required risk retention which is less likely to vary across institutions and eliminates the concerns associated with the disclosures.

Furthermore, if the Agencies decline to make the foregoing change with respect to the timing of the calculation of fair value, we are concerned that providing the disclosures about the underlying assumptions to investors could have the impact of creating an additional level of liability for sponsors that is inconsistent with the purposes of Section 941. This concern is heightened because valuations calculated for purposes of risk retention and valuations calculated for purposes of a sponsor’s books and records will differ due to the application of GAAP at different times and potentially under differing hierarchies. At the very least, the final rule should include a safe harbor from liability for fair value calculations made in good faith and based on good faith assumptions.

*Issues related to the Calculation and Disclosure of “Closing Date Projected Cash Flow Rate” and “Closing Date Projected Principal Repayment Rate”*

The restrictions in the Re-Proposal relating to the calculation of Closing Date Projected Cash Flow Rate (“CFR”) and Closing Date Projected Principal Repayment Rate (“PRR”) raise many of the same concerns as were raised in connection with the premium capture cash reserve account provisions included in the Original Proposal. Under the Re-Proposal, sponsors who retain risk in the form of an EHRI are required to determine the CFR and the PRR prior to the issuance of the EHRI. Such sponsors are also required to certify to investors that pursuant to these calculations the CFR does not exceed the PRR for any payment date.

In many structures these CFR-PRR limitations effectively prevent the EHRI from receiving any payments of interest whatsoever. First loss residual interests in securitizations are by their nature

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<sup>5</sup> Of course, even after pricing there may be various inputs for fair value calculations, as certain ABS Interests may be sold at varying prices, which is often the case for junior tranches.

<sup>6</sup> In iteratively-priced transactions, where pricing occurs over a period of time and a blended final pricing rate is determined, pricing may be determined upon the final pricing of the ABS interests and fair value could be determined at such time based upon the blended pricing rate.

riskier investments as compared to first pay senior interests. Accordingly, market pricing compensates those purchasing residual interests with higher rates of return. Under the Re-Proposal, certain transactions would be restricted from paying any amounts at all to the EHRI, not to mention interest in an amount commensurate with the risk of the investment. The following examples illustrate certain of these concerns:

Example 1: CLO transaction with 48 month reinvestment period:

In this type of transaction, all principal cash flows are re-invested for the initial 48 months of the transaction. The residual interest in this transaction would be prohibited from receiving any cash payments during the reinvestment period, as no principal would be expected to be paid to investors during this time. Even after the conclusion of the reinvestment period, generally a much greater amount of interest is paid than principal, as most CLOs do not have a significant return of principal until close to the final year of the transaction. Therefore, any payment on the residual interest would be extremely limited. The re-proposed rules will make investment in many residual interests economically unviable because investors would not be appropriately compensated for the risk by market terms. Further, even entities with longer term interests, fund managers or other entities that typically invest in these positions, may no longer be able to invest in them, in the odd chance they would still be motivated to do so, due to investment guidelines and/or other applicable criteria or restrictions imposed on them.

Example 2: Typical “conduit” CMBS transaction:

In this type of transaction, the underlying commercial real estate loans are generally structured with an amortization schedule that is much longer than the maturity of such loan. The regular payments made by borrowers under these loans include a large amount of interest and a small amount of principal during the term of the loan with a balloon payment of principal due at maturity. The residual interest in this transaction would be prevented from receiving any meaningful amount of interest payment for an extended period of time, as very limited amounts of principal would flow through the transaction waterfall for the life of the transaction.

Example 3: RMBS Prime Jumbo Transaction-30 Year Term Fixed Rate Mortgage Loans:

In these transactions, senior and subordinate bonds are issued in an amount that equals the aggregate principal balance of the mortgage loans in the pool. For this reason, each senior and subordinate bond generally has a set principal amount and coupon at closing. Because the subordinate bonds are allocated losses first and are generally subordinate in payment priority to unscheduled principal payments (prepayments), they are typically offered with a higher coupon than the senior bonds and/or at a price discount. In a standard transaction, subordinate bonds will receive their proportionate share of



scheduled principal and interest on each distribution date (assuming no losses), but will be locked out from unscheduled principal for a specified period. If the proposed cash flow restriction is put into effect, the subordinate bond representing the retained interest will be prevented from receiving any payments of interest unless prepayments are received because the cash flow restriction will be required to be calculated based on the cash flow (i.e., principal and interest) paid to the subordinate bond in relation to the principal paid to all the bonds.

In this regard, the Re-Proposal makes retention of an EHRI in many structures, such as structures with no or limited principal payments for a period of time or structures with principal reinvestment periods, wholly unworkable, regardless of the fact that senior securities in these structures would continue to receive timely payment of interest and ultimate repayment of principal. Another consequence of limiting the amount of interest payable to the EHRI will be that the EHRI will artificially decrease in value, such that the size of the EHRI required to be retained will have to increase in order to satisfy the 5% fair value requirement.

An EHRI, as a first loss position, would generally impose the most immediate risk of economic loss to the holder of such EHRI. The cash flow limitations imposed by requiring that the CFR never be greater than the PRR could prevent many parties from retaining risk in the form of an EHRI, and therefore decrease the likelihood that parties would be willing to retain risk in this format at all.

With certain modifications, the Agencies' alternative EHRI proposal discussed in the preamble of the Re-Proposal would be a more effective method for addressing the concern raised by the EHRI concept. The alternative EHRI proposal seems to relate to the amount of principal payments received by the residual interest; however, the proposal also states that "the cumulative amount paid to an eligible horizontal residual interest may not exceed a proportionate share of the cumulative amount paid to all holders of ABS interests in the transaction," implying that the intent is to address all cash flows. The preamble goes on to state that "[t]he proportionate share would equal the percentage . . . of the fair value of all of the ABS interests issued in the transaction." Without the benefit of specific proposed rule text it is difficult to discern exactly what type of cash flow comparisons the Agencies are intending in this section of the preamble.

Unless the alternative proposal allows for market rates of return to residual interests, it will also not work for many asset classes. Therefore, we suggest that the alternative proposal be modified to clarify that a residual interest, in order to be considered an EHRI, be limited in the amount of principal repayments it may receive, such that the cumulative amount of payments applied to reduce its principal or notional balance as of any payment date is proportionate to (or less than) the cumulative amount of payments applied to reduce the principal or notional balance of all ABS interests in the transaction as of such payment date. Hence, rather than comparing discounted projected cash flows to the residual holder to actual principal repayments to all ABS interests, the test should focus on a comparison of actual principal repayments to the residual

holder versus actual principal repayments to all ABS interests. The applicable proportionate share would be calculated by sizing the principal or notional amount of the retained interest based on 5% of fair value at the transaction's inception (consistent with the Re-Proposal), and then comparing that amount (which, for example, may be 5.25% of par value) to the principal or notional amount of all ABS interests issued in connection with the transaction. Thereafter, the retained interest would be limited in the amount of payments it could receive to reduce its principal or notional amount, such that it would not be paid down at a faster rate than all senior ABS Interests. By using this measure, the size of the retained interest would never be reduced below the 5.25% that was calculated at inception (assuming no losses).<sup>7</sup>

As such, in a prime jumbo RMBS transaction for example, sponsors would be prevented from allocating principal repayments on the underlying mortgage loans (scheduled and prepayments) at a faster rate to the residual interest than the rate at which such payments would be paid to senior ABS interests, but the residual interest would still be able to receive some cash flows such that it was paid a market rate of return on its investment. Likewise, in a typical "conduit" CMBS transaction, the holders of the EHRI would still be entitled to their market rate of return based on the interest rate paid to such tranche, but the EHRI holder would not be entitled to more than its proportionate share of principal repayments on any payment date during the life of the transaction.

#### Vertical Risk Retention

For sponsors who elect to retain risk via retention of an EVI, calculation and disclosure of fair value should not be required so long as the underlying ABS interests all have either a principal or notional balance. Regardless of whether a sponsor retains 5% of that amount of an ABS interest, or 5% of the fair value of an ABS interest, the resulting amount of retention will be the same.

#### Non-Economic REMIC Residual Interests

We suggest that the Agencies modify the definition of "ABS interest" to specifically exclude "non-economic residual interests" within the meaning of the REMIC rules adopted by the Internal Revenue Service. We believe that requiring sponsors to retain the non-economic residual interest is not within the spirit of Section 941. The non-economic residual interest often has a negative fair value and therefore could actually reduce a sponsor's overall retention. Additionally, a non-economic residual interest is a potential tax liability and unrelated to the credit quality of the underlying collateral.

#### Allocation of Risk Retention to Originators

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<sup>7</sup> There may be particular payment dates where the residual interest did receive a greater proportionate share of principal payments, such as where the residual interest is allocated recovery amounts for prior losses, but this would be consistent with Section 941 as losses would first be allocated to the EHRI and its repayment rate would never be greater than the senior ABS Interests issued in connection with the transaction.

The 20% threshold for a sponsor's ability to allocate a portion of its risk retention to an originator should be eliminated. The Re-Proposal requires that any originator acquire and retain at least 20% of the aggregate risk retention amount otherwise required to be retained by the sponsor. This 20% threshold remains too high and is unnecessary and inconsistent with the goals of the Re-Proposal. This regulation will result in smaller originators, those that are unable to produce or hold assets at a rate that allows them to aggregate enough assets to satisfy the 20% threshold, finding their portfolios to be less liquid and the sale of their assets to be at prices that are less favorable. In the extreme, these smaller originators may be pushed out of the market entirely and an important part of the capital that supports these capital markets will be eliminated. Additionally, this threshold is inconsistent with the objectives of the Re-Proposal. A smaller originator is responsible for underwriting the assets that it contributes to a particular transaction, regardless of its proportionate share of a particular transaction. The allocation of the proportionate share of risk retention to such originator supports the goal of the Re-Proposal without imposing any artificial thresholds. An originator, no matter its contribution to a particular transaction, would be responsible for retaining its proportionate share of the risk and this retention would encourage sound underwriting practices by such originator. Accordingly, we support the position taken by SIFMA/FSR/ABA/ABASA and others in the industry that the 20% threshold should be eliminated.

## **V. OTHER ASSET CLASSES**

### **A. Autos, Credit Cards and Student Loans**

Wells Fargo has not historically been, and is not currently, a large sponsor of auto loan, credit card or student loan securitizations ("Consumer ABS"). However, as a large originator of auto loans, credit card receivables and student loans we understand the need for, and are very interested in, the efficient operation of the Consumer ABS market. In addition, through our broker-dealer, Wells Fargo facilitates access to liquidity via the capital markets which is a critical source of capital to the consumer finance market. Ultimately, we are concerned with the availability of credit to consumers and we understand that a properly functioning securitization market together with the bank balance sheet funding that we and other financial institutions provide is critical to the U.S. economy.

Various industry and lobbying groups, including SFIG and SIFMA/FSR/ABA/ABASA are filing detailed responses to the Re-Proposal as it relates to Consumer ABS. While we agree that risk retention is one way to help ensure a properly functioning Consumer ABS market, we also strongly agree that further revisions and clarifications are necessary to ensure that the Re-Proposal does not damage the securitization market generally, and the Consumer ABS market specifically. The Re-Proposal addresses many of the issues raised by the various commenters to the Original Proposal, however, there are issues that if not addressed will have a detrimental impact on Consumer ABS, which will further limit and constrain the availability of credit for families and businesses. One example is the qualifying auto loan concept ("QAL"), which

provides a welcome exemption from the risk retention requirements. However, the QAL criteria are overly restrictive and not reflective of how auto loans are currently originated and, therefore, the exemption is of little or no value to the auto loan securitization market. This was clearly not the intention of the Agencies and properly aligning the QAL criteria with how auto loans are currently originated should be addressed in any final rule. Wells Fargo has worked closely with SFIG and SIFMA/FSR/ABA/ABASA in reviewing the Re-Proposal and we endorse the respective comment letters filed by those trade organizations as it applies to Consumer ABS. As those letters are still in progress, to the extent our comments ultimately materially differ substantially from those of SFIG or SIFMA/FSR/ABA/ABASA we will provide our own comments in a supplementary submission.

### **B. Resecuritizations and Repacks**

Wells Fargo has worked closely with SIFMA/FSR/ABA/ABASA and SFIG in reviewing the Re-Proposal as it relates to resecuritizations and repackaging transactions and endorses the respective comment letters filed by those trade organizations. Wells Fargo participates in these markets mainly by assisting clients in tailoring and managing their investments to meet their individual needs. For example, a client holding a legacy RMBS position may desire to reduce its exposure to the position by selling off a portion of the risk associated with that asset to an institutional third party investor. Or an institutional money manager may wish to eliminate interest rate risk on a fixed rate corporate bond by converting to a floating rate interest payment stream. These types of products involve underlying assets which have been purchased in the secondary market. We continue to believe that applying the risk retention requirements to them will have no impact on the origination or underwriting of the underlying assets, but rather will serve to limit investors' ability to manage their existing exposure or tailor their investments by removing or severely limiting the availability of these effective tools. The availability of resecuritizations during the downturn proved to be critical to banks and non-bank financial institutions in their efforts to manage risk. The negative impact of the Re-Proposal will be most evident during any future economic downturn.

### **C. Tender Option Bond Programs**

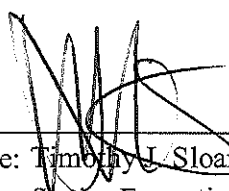
We appreciate the Agencies' efforts to address the issues related to TOBs in the Re-Proposal. As noted above, Wells Fargo has worked directly with Ashurst LLP and a majority of the TOB sponsors in the preparation of a separate comment letter addressing concerns with the Re-Proposal specifically in the context of TOBs. We have also worked with SFIG on the preparation of its comment letter as it relates to TOBs. We endorse each of these letters and look forward to working with the Agencies in addressing these concerns.

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Wells Fargo supports the Agencies efforts to properly align the incentives of the various participants in the securitization market and instill more discipline in the credit origination process by enacting risk retention rules. We also appreciate the Agencies' efforts to address and accommodate many of our previously submitted comments. The Agencies' efforts to instill discipline in the securitization market must be appropriately balanced so as to allow that market to serve the important function of providing liquidity to the U.S. economy. If the risk retention rules do not achieve such balance, or if the disincentives to securitization become too great, such rules will have a crippling impact and consumers and businesses will suffer. As we stated in our 2011 letter, we believe that a carefully crafted risk retention rule could be an important tool in achieving a proper alignment of incentives and disciplined credit origination, and our goal in this submission is to further assist the Agencies in this endeavor.

If you have any questions or would like to discuss our commentary further, please feel free to contact me.

WELLS FARGO & COMPANY

By:  \_\_\_\_\_

Name: Timothy J. Sloan

Title: Senior Executive Vice President and  
Chief Financial Officer