March 14, 2013

Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002, Basel
Switzerland

Re: Consultative Paper: "Revisions to Basel Securitisation Framework"

Ladies and Gentlemen:

The American Securitization Forum ("ASF")[1] appreciates the opportunity to provide comments to the Basel Committee on Banking Supervision (the "Committee") on the consultative paper, "Revisions to the Basel Securitisation Framework" (the "Consultative Paper"), released on December 18, 2012.[2] The Consultative Paper addresses proposed revisions to the securitization framework for regulatory capital requirements.

The financial crisis made apparent that regulatory capital rules for banks were in need of reform. The ASF has commented extensively to the Committee and to the Board of Governors of the Federal Reserve System (the "Federal Reserve"), the Office of the Comptroller of the Currency (the "OCC") and the Federal Deposit Insurance Corporation (the "FDIC" and, together with the Federal Reserve and the OCC, the "U.S. Agencies") on Basel III and other aspects of reform to the regulatory capital rules.[3] We confirm again, as we have in each comment letter addressing

[1] The American Securitization Forum is a broad-based professional forum through which participants in the U.S. securitization market advocate their common interests on important legal, regulatory and market practice issues. ASF members include over 300 firms, including issuers, investors, servicers, financial intermediaries, rating agencies, financial guarantors, legal and accounting firms, and other professional organizations involved in securitization transactions. ASF also provides information, education and training on a range of securitization market issues and topics through industry conferences, seminars and similar initiatives. For more information about ASF, its members and activities, please go to www.americansecuritization.com

[2] *See* http://www.bis.org/publ/bcbs236.pdf.

[3] *See* http://www.americansecuritization.com/ASF_Comment_Letter_on_Reg_YY_NPR_4_29_12.pdf for Letter from ASF to the Federal Reserve, dated April 29, 2012, regarding the notice of proposed rulemaking implementing enhanced prudential standards and early remediation regulations under Sections 165 and 166 of Dodd-Frank. *See* http://www.americansecuritization.com/WorkArea/DownloadAsset.aspx?id=8342 for Letter from The Clearing House and ASF to the Federal Reserve, FDIC and OCC, dated October 22, 2012, regarding the three notices of proposed rulemaking implementing the capital related provisions of Basel III and certain aspects of the Basel II standardized approach. (the "Association Basel III Comment Letter").

capital proposals, that our members strongly support robust capital requirements, both as to the components of regulatory capital and required minimum levels.

Revised capital requirements for securitization exposures must, however, be appropriate for the risks associated with these exposures. Increasing the capital requirements for securitization exposures to levels that are well above what is necessary, given the risks of these exposures will unnecessarily discourage banks from being active participants in the securitization market. Other regulatory changes implemented and proposed in the securitization markets and structural changes to securitizations since the financial crisis, including changes to ratings criteria, have and will correct many of the historical issues in these markets that concern the Committee without the need for additional capital requirements beyond those that have been proposed by the Committee in the past and that are in effect or are in the process of being implemented by banks generally.[4]

Banks are among the largest investors in mortgage-backed securities ("MBS") and asset-backed securities ("ABS") globally. Research demonstrates that robust securitization markets contribute significantly to economic growth and recovery.[5] Almost every significant consumer and commercial asset requires financing and securitization is a substantial source of that financing. Given the prominent role that banks play in the availability of that financing, capital requirements for securitization exposures must be set at levels that appropriately account for the risks *and benefits* of using securitization as a financing method and that encourage banks to continue to be important participants in the securitization market.

The ASF has consistently indicated that the following "guiding principles" should be embodied in any framework for determining capital for securitization exposures. Any securitization capital framework should:

- promote understanding by banks of the risks associated with their securitization exposures;

- focus on (i) actual performance of assets, which is the primary driver of the performance of a securitization exposure, and (ii) the credit support available to a

[4] Fitch Ratings indicates that it expects that total losses on structured finance bonds issued between 2000 and 2011 and rated by Fitch will be less than 5% and that pre-2008 ABS transactions account for 99% of total projected losses. According to Fitch Ratings, "…pre-crisis transactions benefit from higher credit quality, and greater credit protection." *See* Fitch Ratings, "Proposed Basel Framework Inconsistent with SF Performance" (December 21, 2012).

[5] In arguing that the proposed changes to the securitization capital framework will have an enormous impact on the viability of the securitization business and also on the broader economy, Deutsche Bank cites to the U.S. CMBS and U.S. auto loan ABS markets. According to Deutsche Bank, the re-emergence of a strong new issue CMBS market in the U.S. has contributed to nearly a complete recovery of commercial property values in major markets and, over the last ten years, the amount of cars sold in the U.S. has exhibited nearly a perfect correlation to the balance of related ABS issuance. *See* Deutsche Bank, The Outlook, "CRE and Consumer ABS: Tougher Basel III Proposal puts CMBS and ABS at Risk" (February 27, 2013).

given risk position within an securitization structure after factoring in the assets' performance;

- function to facilitate dynamic and timely adjustment of capital in a manner that is consistent with and proportionate to changes in asset performance and the resulting risk profile of a given exposure; and

- be premised on data that is available to all market participants and should otherwise comport with standard market practices.

An international capital framework should also assure, to the greatest extent possible, consistency of capital charges for identical securitization exposures as between different banks and across jurisdictions. Our comments on the Consultative Paper set forth in this letter are intended to align any revised framework for determining capital for securitization exposures with these guiding principles.

Part I of this letter is an executive summary of our comments; Part II discusses the need for a second consultative paper; Part III sets forth comments on the proposed hierarchies; Part IV sets forth comments on the proposed MSFA; Part V sets forth comments on the proposed RRBA; Part VI sets forth comments on the proposed SSFA; Part VII sets forth comments on the proposed concentration ratios; Part VIII sets forth comments on the definition and treatment of re-securitization exposures; Part IX sets forth comments on the 1,250% maximum risk weight; Part X sets forth comments on the maximum capital charge (overall cap); Part XI sets forth comments on the maximum risk weight for senior securitization exposures; Part XII sets forth comments on early amortization provisions; and Part XIII sets forth comments on the treatment of write downs and purchase discounts.

I. EXECUTIVE SUMMARY

The ASF has significant concerns with a number of aspects of the Consultative Paper. These concerns stem from our belief that the Consultative Paper is inconsistent in many respects with the guiding principles discussed above.

The ASF is of the firm belief that where possible, banks should use the same methodology for determining the capital charges for securitization exposures. The use of different methodologies will by definition lead to different capital outcomes for different banks located in different jurisdictions. The ASF believes this result should be avoided wherever possible.

The ASF realizes, however, that the use of different methodologies inherently creates the inconsistencies we believe a risk-based capital framework should seek to avoid. Therefore, a significant thrust of our comments is focused on the Modified Supervisory Formula Approach ("MSFA"). First, we are of the view that the MSFA should be at the top of any securitization capital framework hierarchy. Second, we believe its potential use should be expanded to any bank that has the information necessary to determine capital charges using the MSFA. Third, we

believe that portfolio inputs should be permitted to be used in appropriate circumstances in order to expand the scope of the practical usability of the MSFA by banks that invest in securitization exposures. Fourth, we believe the MSFA in its current form results in a systemic overstatement of capital charges for securitization exposures and should be adjusted in ways that we propose herein to produce capital charges that are more in line with the actual risks of securitization exposures in different economic conditions.

We believe that the other methodologies proposed in the Consultative Paper should be used only if the MSFA is unavailable as a method for determining capital. The ASF also believes that these methodologies should produce capital outcomes that are correlated as closely as possible to capital charges that would be produced using the MSFA. We have therefore suggested certain changes to these methodologies that would produce capital outcomes that are more consistent with the MSFA after giving effect to our proposed modifications.

Given that concentration ratio approaches do not produce capital outcomes that correspond to the credit quality of the underlying asset pool and the availability of credit enhancement, we believe that their use should be rare. We are particularly concerned that the Backup Concentration Ratio Approach ("BCRA") is the only method available for determining capital for re-securitization exposures. We believe that the more risk sensitive methodologies should be available for re-securitizations. We also believe that in the event that the Committee continues to insist that the BCRA be the only method available to re-securitizations, that certain securitization exposures should be excluded from the definition of re-securitizations.

Finally, the ASF is making certain other comments to specific aspects of the Consultative Paper that are designed to produce more logical and sensible capital charges for securitization exposures. First, the 1250% maximum risk weight should be capped at the dollar amount of the bank's exposure, since capital should never be more that a bank's maximum exposure to the risk of an asset. Second, the scope of the proposed caps on overall capital and on the amount of capital for senior exposures should be expanded and clarified in order to produce consistent capital charges as between securitized and unsecuritized assets across banks. Third, with appropriate safeguards, banks should be permitted to treat exposures to securitizations with early amortization features as securitization exposures. Finally, the carrying value of an exposure should be taking into account when determining the available credit enhancement for an exposure.

Our principal objective in making these comments is to contribute to the development of a capital framework that produces capital outcomes for securitization exposures that are both conservative and promote the continued use of securitization in appropriate circumstances as a financing tool that promotes economic growth and prosperity. We look forward to our continued discussions with the Committee on these issues.

II. THE COMMITTEE SHOULD PROPOSE A REVISED COMPREHENSIVE CONSULTATIVE PAPER

The Consultative Paper sets forth a framework for determining capital for securitization exposures that is substantially different from the existing framework and from changes to that framework that are only now being implemented by means of regulation by banking supervisory authorities. The time period our members have been given to respond to these changes has been extremely short given the scope of the proposed changes and our comments have not been informed by the results of the quantitative impact study ("QIS") that the Committee is undertaking.

The Consultative Paper also does not address the treatment of securitization exposures in the trading book. The Committee indicates that, since a fundamental review of the trading book rules is underway, it is not proposing specific changes to the trading book rules at this time. The Committee also indicates, however, that it supports the principle that opportunities for regulatory arbitrage should be avoided. Our members therefore fully expect that changes to the trading book rules for determining capital for securitization positions will be broadly similar to whatever changes to the securitization framework ultimately result from the consultative process. Our members are therefore of the view that the Consultative Paper should have addressed trading book issues.

In light of these factors, we strongly urge the Committee to publish a second consultative paper that addresses industry comments and concerns and the results of the QIS and that addresses trading book issues. We look forward to such a second paper and the opportunity to address in a comprehensive and meaningful way the changes to the securitization capital framework outlined in the Consultative Paper and that we expect to be meaningfully refined in such a second paper.

III. THE PROPOSED HIERARCHIES

A. The ASF supports the adoption of Alternative A.

Alternative A is a better hierarchy of approaches for calculating the capital of securitization exposures than Alternative B. Alternative B requires the use of BCRA for all exposures other than "high quality securitization exposures." As discussed further below, a concentration ratio ignores the positive effects of asset overcollateralization and is also insensitive to the risks inherent in the securitized exposures. The resulting contrasts in risk weights between senior and subordinated securitization exposures and between securitizations of high quality senior exposures and relatively lower quality exposures is not warranted in many transactions.

In contrast, Alternative A would permit the use of the MSFA, RRBA or SSFA for all exposures other than re-securitizations, thus recognizing the positive effects of credit enhancement in determining risk weights. This will avoid significant differences in risk weights between senior and subordinate tranches in securitization tranches that may not be warranted by the actual credit risk of these exposures. It would also allow significant differences in the credit quality of asset

pools underlying securitization exposures to be taken into account under the MSFA, RRBA and, if our proposed modifications are adopted, the SSFA.

Although Alternative A is better than Alternative B, Alternative A is not perfect. It does not permit the use of one of the approaches that recognizes the effects of credit enhancement for re-securitization exposures. As discussed further below, this would result in a significant overstatement of capital for many high quality re-securitization exposures.

A key factor in our support of the adoption of Alternative A is the assumption that the Committee is amenable to making the MSFA available for more securitization exposures as set forth below. While we propose changes to each of the MSFA, RRBA and SSFA below, we recognize that because of the differences of inputs to the approaches and other factors that the three approaches can never be perfectly correlated. The best result in our view, therefore, is to allow the MSFA to be used more often in situations where the bank is an investing bank under the conditions described below. The MSFA is the most risk sensitive of all of the approaches and should be used whenever possible to calculate the risk weights of securitization exposures. Making changes to cause it to be available in as many situations as possible will assure more uniform capital treatment across banks and across jurisdictions given its position at the top of the Alternative A hierarchy.

IV. THE PROPOSED MSFA

A. Any bank that has access to the inputs necessary to calculate the capital of a securitization exposure under the MSFA should be permitted to use this approach.

The Committee should expand the permitted use of the MSFA as a capital calculation method to the securitization exposures of all banks. Given that the MSFA is the most risk sensitive of the approaches set forth in the Consultative Paper, all banks that have the data available to calculate K_{IRB} and the other inputs necessary to calculate the MSFA should be permitted to determine the capital of their securitization exposures using the MSFA. Given that, once the inputs necessary to calculate the MSFA are obtained, the MSFA is in essence a mathematical calculation, there does not seem to be any logical or significant policy reason not to permit Standardized Approach banks to use it. In fact, expanding the use of the MSFA to Standardized Approach banks would by definition promote consistency in risk weights for securitization exposures across banks and across jurisdictions, which should be a primary goal of any securitization capital framework.

B. Banks should be permitted to assign pool wide risk parameters in determining K_{IRB} for securitization exposures to highly granular, homogeneous asset pools.

The Committee proposes to restrict the use of the MSFA to securitization exposures for which a bank can develop IRB parameter estimates for each of the assets underlying the securitized pool. However, the asset-level information required to calculate the probabilities of default ("PDs") and losses given default ("LGDs") of individual wholesale exposures and retail exposures for purposes of calculating K_{IRB} is not available to a bank that invests in a securitization exposure

unless the bank originated the underlying assets and continues to act as the servicer of those assets. Otherwise, U.S. federal securities laws do not currently require issuers of asset-backed securities to disclose asset-level information to investors and, in many instances, the issuer is not a bank and may not track the necessary information on an asset-level basis.[6]

To not allow the use of pool-wide parameters for calculating K_{IRB} under the MSFA in these circumstances curtails the use of the MSFA to situations where a bank has originated the securitized assets or can negotiate for access to exposure-by-exposure information on the underlying pool assets. Restricting the use of the MSFA in this manner would seem to cut against the Committee's stated goal of reducing mechanistic reliance on credit ratings, since it virtually ensures that banks will use the RRBA for determining risk weights in jurisdictions that permit such use. Further, as discussed above, allowing the MSFA to be used in more transactions where a bank invests in a securitization exposure under appropriate conditions would also promote more uniformity in capital treatment across banks and jurisdictions.

Therefore, the ASF proposes that banks be permitted to use the MSFA to calculate capital on a portfolio basis for securitization exposures to homogeneous asset pools that consist of at least 100 underlying exposures, using portfolio data such as the average PD and LGD of the portfolio and a correlation value consistent with the average PD. As long as banks investing in securitization exposures use pool wide proxies for these inputs and update these proxies periodically to reflect asset performance, there does not seem to be any significant policy reason to prohibit these banks from determining capital using the MSFA. Using pool wide proxies for securitizations of the type which we propose would result in a conservative K_{IRB} calculation given the similarity among the pool assets and the fact that the actual credit quality of any given pool asset would not have a significant effect on the credit quality of the pool as a whole. We can demonstrate that in virtually every case, the simpler portfolio wide approach is considerably *more* conservative, *i.e.* results in a higher capital calculation, than the approach based on calculations performed at the individual asset level.

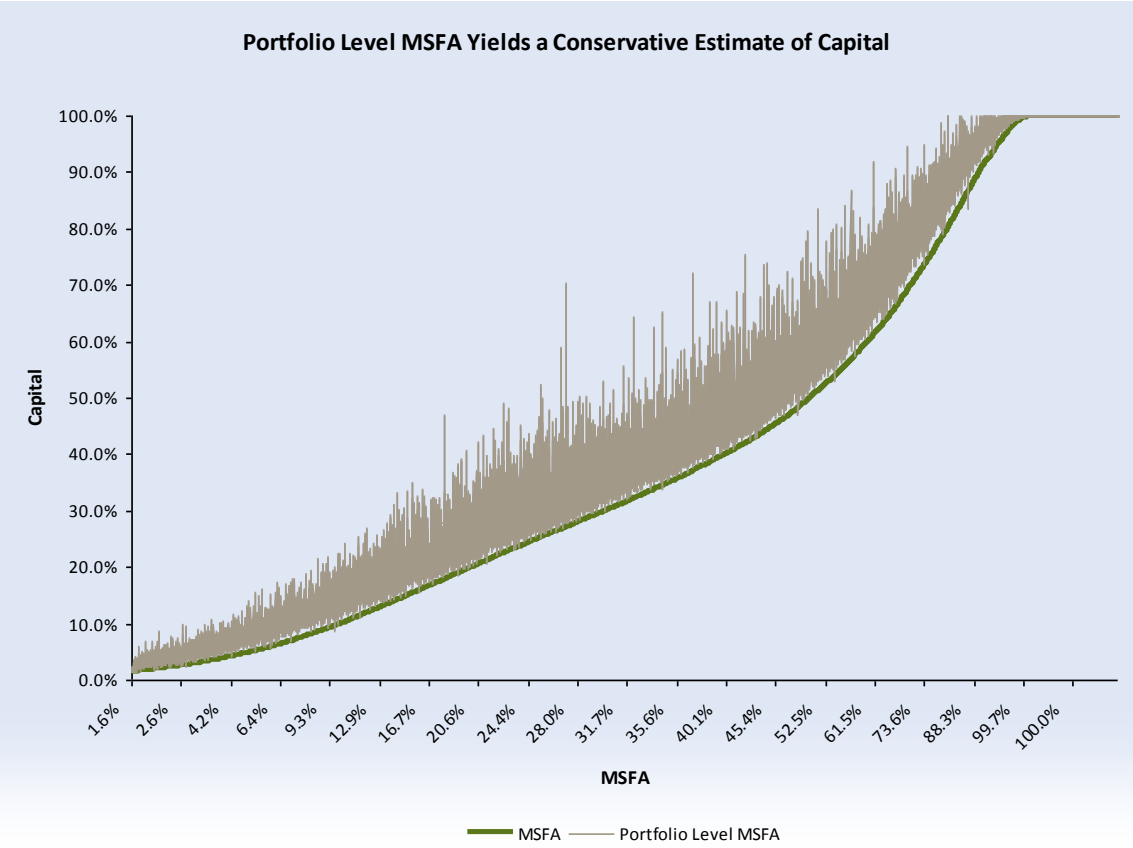
We performed a simulation analysis of 50,000 samples that created random tranches with a wide variety of characteristics as follows:

- 100 underlying exposures with random notional amounts over a 0-1000 range
- PD values randomly assigned from 0 to 30% for each of the 100 underlying

[6] ASF expects U.S. asset-level disclosure to evolve through new proposed requirements arising out of the Dodd-Frank Act and the SEC's proposal of Regulation AB II. *See* http://www.americansecuritization.com/ASFRegABIICommentLetter8.2.10.pdf for ASF's August 2, 2010 broad Reg AB II response letter, http://www.americansecuritization.com/ASFRegABIIABCPCommentLetter8.2.10.pdf for ASF's August 2, 2012 ABCP Reg AB II letter, http://asf.informz.net/asf_reg_ab_ii_auto_abs_comment_letter_8.31.11.pdf for ASF's August 31, 2010 Reg AB II Auto Disclosure comment letter, http://www.americansecuritization.com/ASF_Reg_AB_II_Waterfall_Comment_Letter_8.31.10.pdf for ASF's August 31, 2010 Reg AB II Waterfall comment letter, and http://www.americansecuritization.com/ASF_Comment_Letter_on_SEC_Reg_AB_II_Re-Proposal_10-4-11.pdf for ASF's October 4, 2011 comment letter in response to the Reg AB II Re-Proposals.

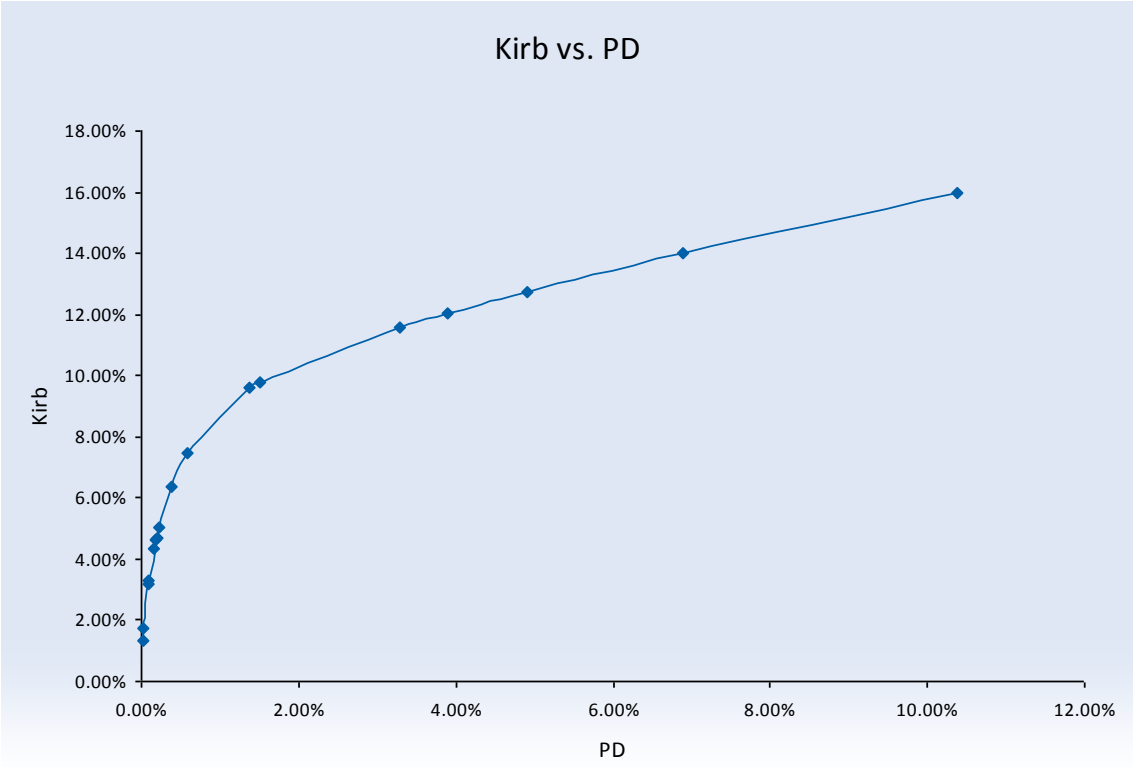
- LGD values randomly assigned from 0 to 100% for each of the 100 underlying
- AVC values calculated as a function of the PD values per the IRB approach
- Attachment points varying randomly from 0 to 50%
- Detachment points varying randomly from attachment + 1% to 100%

We find that in 99.9% of cases the portfolio level calculation results in a higher capital allocation. The ratio between the portfolio level result and the standard MSFA result averaged 124%. See Graph 1 below:



Graph 1

In addition, a purely mathematical argument can be made on the basis of the relationship between K_{IRB} and the probability of default variable. The K_{IRB} curve levels off as the PD goes up, so the higher risk names contribute "less than linearly" to the total capital (see Graph 2 below). Or in other terms, the second derivative of the K_{IRB} with respect to PD is always negative. As a result, using the average PD can never result in a lower K_{IRB} than the approach where the underlying exposures are individually analyzed.



Graph 2

As a result of this relationship, it would seem reasonable to allow sophisticated market participants to make use of portfolio level inputs to calculate the K_{IRB}, and therefore also make use of the MSFA to calculate the regulatory capital for securitization exposures. This approach would have many desirable characteristics:

- It does not rely on credit ratings;
- It requires fewer estimations than the MSFA as proposed in the Consultative Paper;
- It requires less modeling than the MSFA as proposed;
- It could not be "gamed" in order to create a specific capital outcome; and
- It would promote transparency in the market by creating a demand for timely and accurate portfolio level loss data from asset originators. This is consistent with the intentions of securitization disclosure regimes including the U.S. Securities and Exchange Commission's Regulation AB.

To assure that banks making use of pool-wide parameters to determine capital charges using the MSFA are qualified to do so, the Committee could subject such banks to an approval and review process similar to thet process that applies under the Basel II framework to banks using the

Internal Assessment Approach ("IAA").[7] As with the IAA, a bank's primary supervisory authority could be required to approve the processes and methodologies that a bank uses to determine pool-wide inputs in determining capital using the MSFA, could subject these processes and methodologies to regular audits and reviews, and could prohibit the bank from continuing to use pool-wide inputs if these processes and methodologies were no longer considered adequate.

Additionally, banks are currently permitted to assign risk parameters to segments of retail assets and to segments of wholesale assets with maturities of less than one year in determining K_{IRB}. In order for the MSFA to be a viable option for banks investing in securitization transactions, this permitted segmentation must continue under the MSFA and should be expanded by removing the one year cap for wholesale assets that applies under the current version of the SFA.[8] Further, in situations where the use of pool-wide proxies would not be permitted and the bank has the data to calculate K_{IRB} for a substantial portion of the underlying assets or asset segments, banks should be permitted to use conservative PD and LGD proxies for the remaining exposures in order to use the MSFA to determine capital for such exposures. To require a bank to use a less risk sensitive approach to determining risk weights in these circumstances seems an unduly harsh result. We would propose in these circumstances that the Committee adopt an approach to this issue that has been adopted for certain eligible wholesale exposures with maturities of less than one year by the U.S. regulators in the U.S. version of the Advanced Internal Ratings-Based Approach. U.S. banks may use the expected credit loss ("ECL") of such an exposure divided by it's exposure at default ("EAD") as a proxy for a PD for these assets and are required to assume a 100% LGD.[9]

C. The MSFA as proposed results in systemic overcapitalization of securitization exposures. The MSFA should be revised to (i) recognize the positive effects of margin income received on longer maturity assets in calibrating a maturity adjustment to the MSFA, and (ii) adjust the risk weight floor to a level that results in capital charges for securitization exposures that are more realistic given their actual levels of potential risk.

Overview

In this analysis, we identify four categories of conservatism that give rise to systemic regulatory overcapitalization in the Basel III MSFA calculation.

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[7] Basel II: International Convergence of Capital Measurement and Capital Standards: A Revised Framework - Comprehensive Version, Part 2: The First Pillar- Minimum Capital Requirements (June 2006).

[8] Our members do not see why a bright-line one year cut off should apply in these circumstances. The wholesale framework includes a maturity adjustment, which would result in more conservative K_{IRB} calculations for longer term securitized asset pools.

[9] *See* Agencies, Risk-Based Capital Standards: Advanced Capital Adequacy Framework-Basel II; Final Rule (72 Federal Register 69288, at 69332, December 7, 2007).

1. Elements "baked into" the MSFA formulation that accumulate through various conservative assumptions, sometimes referred to as prudential add-ons;

2. Conservatism added as a result of the re-specification of the tau and omega parameters;

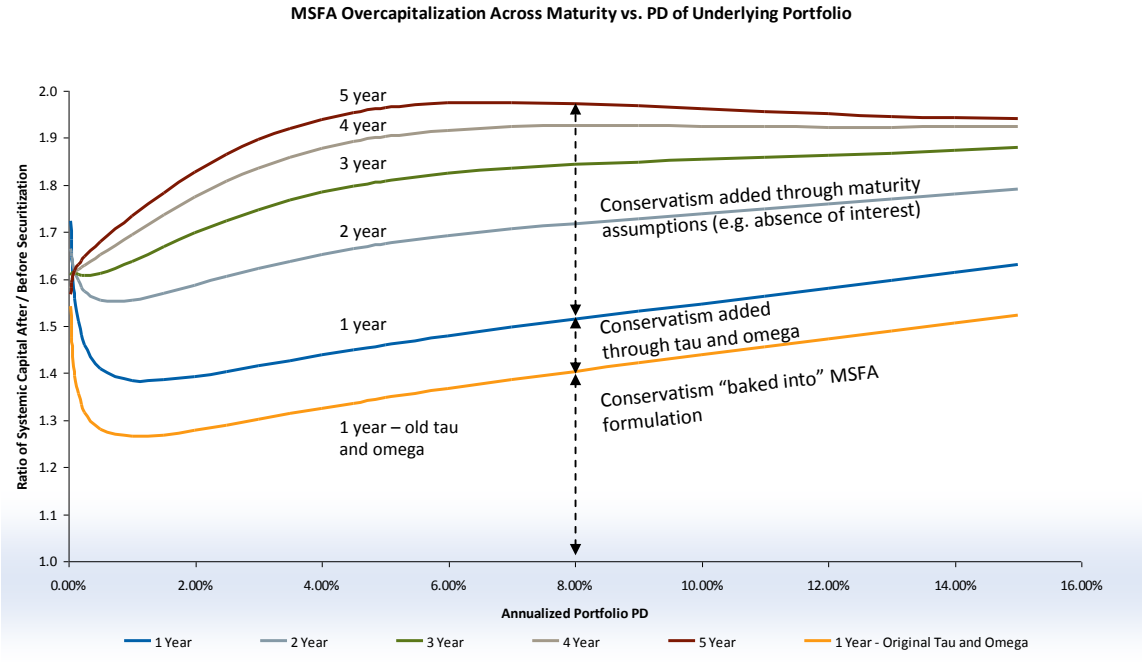
3. Conservatism that is a function of the treatment of maturity, likely the result of the assumption that there is no interest income thrown off by the underlying assets after year one; and

4. Conservatism added by the superimposition of the 20% risk weight floor.

This overcapitalization results in the systemic regulatory capital after securitization being multiples of the capital before securitization, viewed as a sum across the entire capital structure.

Impact of Maturity on MSFA results

Graph 3 displays the result of an analysis taken across a broad range of values for PD, assuming a 30% LGD and before the introduction of the 20% risk weight floor. The values in the graph represent the multiple of systemic capital (*i.e.,* capital after securitization divided by capital before) that results from the implementation of the MSFA. The results describe the impact of three categories of conservatism, those "baked into" the MSFA, the tau and omega factors and the impact of maturity.



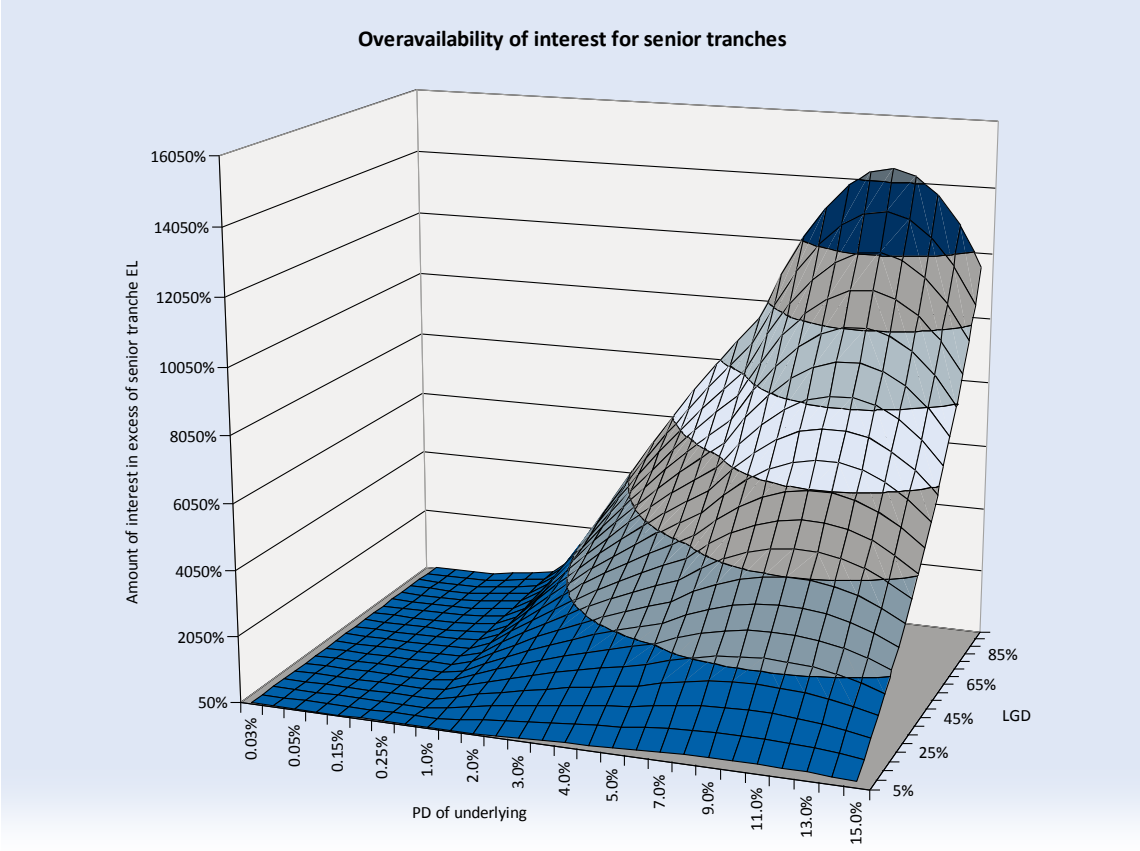
Graph 3

Prudential add-ons appear to be responsible for causing capital after securitization to be at least 1.25 times capital before securitization. The re-specification of tau and omega contribute

another 10% increase, and, as we go from 1 to 5 years in term, the degree of overcapitalization increases to nearly 2 times. We believe this is a result of the assumption made in the MSFA implementation that the underlying portfolio of assets throws off no interest after year 1. Paragraph 18 of "Working Paper No. 22 - Foundations of the Proposed Modified Supervisory Formula Approach" from January 2013 includes this text:

> *. . . IRB Pillar 1 charges assume, in effect, that expected default losses beyond the capital horizon will be covered by margin income or excess spread. This assumption was problematic for many securitisations during the financial crisis, as sharp deteriorations in the underlying pools eroded anticipated excess spread. A key difference between the IRB framework for wholesale exposures and the MSFA framework is that the latter does not provide any capital benefit for excess spread. For maturity exceeding one year, this difference in the treatment of excess spread is one of several reasons why the sum of MSFA charges across all tranches of a securitisation would tend to exceed the IRB charge for the underlying pool, even abstracting from the proposed MSFA's prudential add-ons.*

This assumption is quite conservative and is certainly at odds with the facts of securitization structures as they relate to senior tranches. The senior-most tranches will be the beneficiary of more than their pro rata share of the interest thrown off by the underlying portfolio of assets, far more than enough to pay for the expected losses on those tranches. Our analysis shows a minimum of 70% more interest than necessary to pay for the expected losses of the senior tranche, given the common securitization structures that divert interest to the senior tranches first.

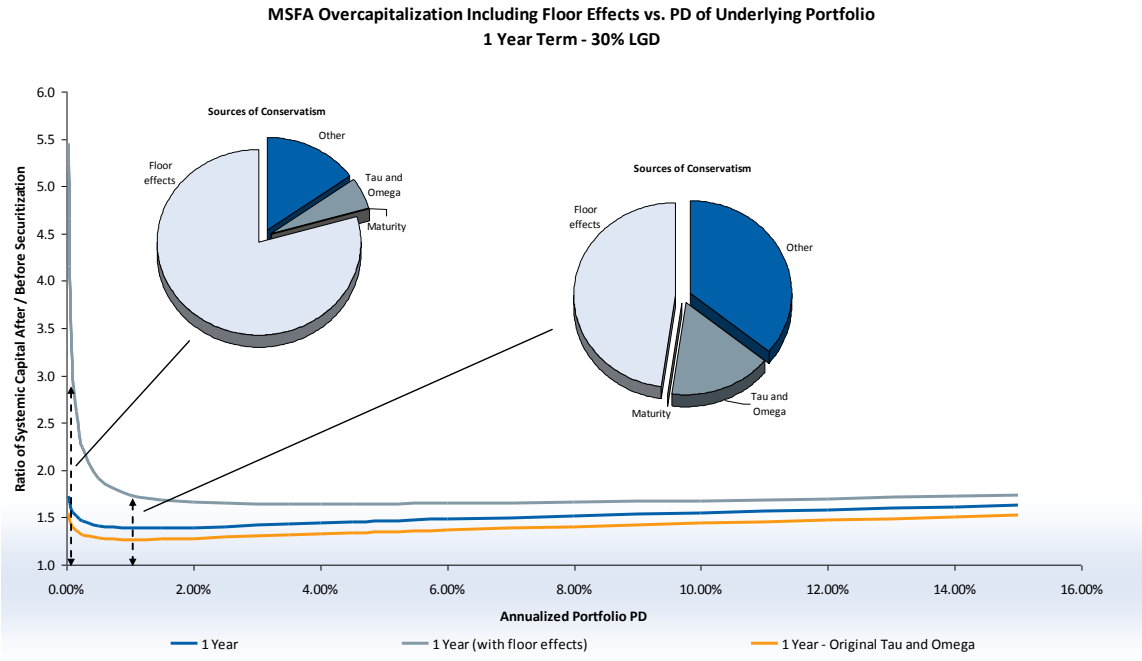


Graph 4

We feel there is strong evidence to support the contention that at least for senior tranches, the assumption of no interest past year 1 be relaxed. This should have the effect of reducing the amount of overcapitalization attributable to the maturity adjustments for these positions.

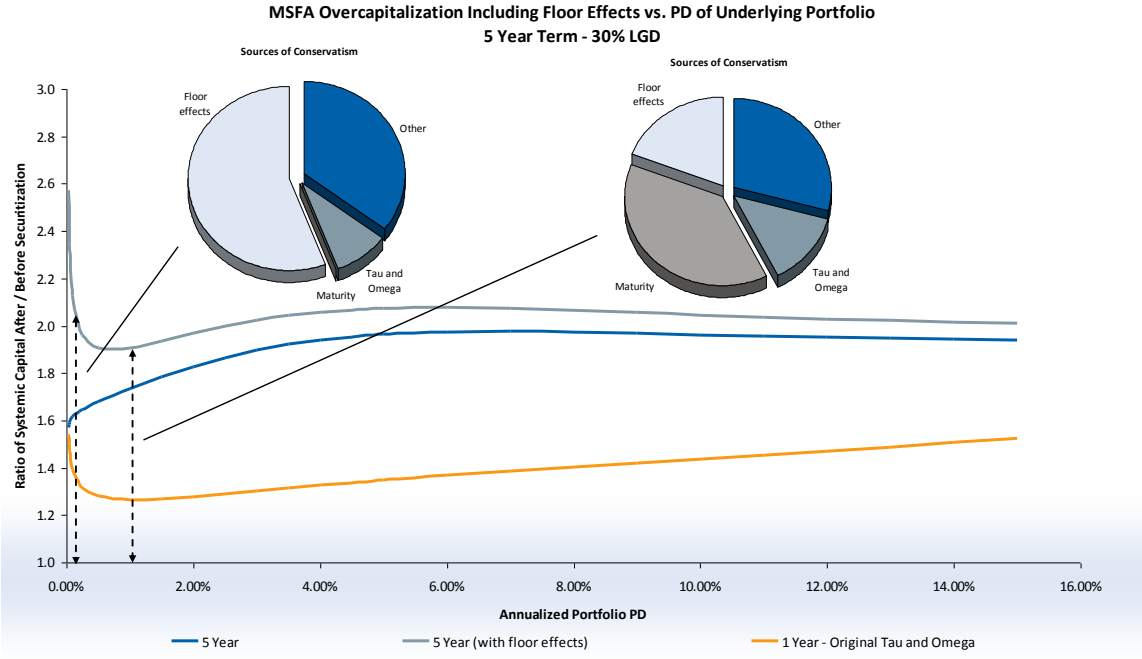
Impact of Risk Weight Floor

Another key source of overcapitalization is the risk weight floor of 20%. Graphs 5 and 6 extend the analysis to include the impact of the floor and display the relative contribution to this overcapitalization attributable to each of the four elements: Prudential add-ons, tau/omega, maturity and floor. For the lowest risk portfolios, the floor becomes the driving factor to overcapitalization multiples that can exceed 10x. Graph 5 shows these effects for a broad spectrum of PD assumptions at the 1 year point, assuming a 30% LGD. The floor dominates the results.



Graph 5

Graph 6 displays the impact at the 5 year point, where the floor has less of an impact, due to the inflation of the results that can be traced to the maturity assumptions.



Graph 6

Conclusion

The analysis would tend to support the proposal to relax the assumption of no interest generated past year one, at least for the senior tranches of securitization. In addition, the analysis suggests that results are distorted for the lowest risk portfolios by the imposition of the 20% floor, generating systemic overcapitalization on an unrealistic scale.

D. If the maturity adjustment set forth in the proposed MSFA is not calibrated as described above, it should be based on the weighted average expected maturity of the underlying assets.

The weighted average expected maturity of the underlying assets is a more meaningful measure of maturity than the contractual maturity of the underlying assets. Basing a maturity adjustment on the contractual maturities of the underlying assets, or lacking that, the legal final maturity of the relevant securitization tranche, overstates the practical maturity of a tranche by ignoring the effect of actual asset cash flows (and in some cases asset prepayments) on the repayment of a securitization tranche.

It should in any event be made clear that banks may use contractual maturities where available in determining the proposed maturity adjustment. While we believe that this is the Committee's intention, there are several instances in the Consultative Paper where this is less than clear. In nearly all cases, the legal final maturity of a securitization tranche is set at a point in time that is well beyond the latest contractual maturity of any asset in the underlying pool. This is done in amortizing transactions to assure that an end date exists at which point investors in the securitization may foreclose on delinquent and defaulted underlying collateral to permit an orderly disposition of the related asset pool. If that date were set too close to the last asset contractual maturity, it would interfere with the benefit of the issuer's bargain, namely that investors in the securitization will receive distributions if and when payments on the underlying assets are made.

E. Banks must be able to take into account the credit enhancing effects of excess spread for certain asset classes in order for risk-weights determined under the MSFA to correlate with risk weights determined under the RRBA.

Neither the proposed MSFA nor the SFA in its current form recognizes additional credit enhancement available to a securitization position from cash flows on securitized assets. The inability to recognize such cash flows can substantially understate credit enhancement for many securitizations, including credit card and auto loan securitizations. This creates inconsistencies in risk-weights for identical securitization exposures as between the MSFA and the RRBA, because the credit ratings used in the RRBA recognize the impact of excess cash flows on the creditworthiness of a securitization position.

The ASF therefore proposes that banks using the MSFA be permitted to use cash flow analyses to determine the additional credit enhancement that is inherent in transaction cash flows but is not recognized by subordinate securitization positions. In order to assure the integrity of such cash flow calculations, the ASF proposes that excess cash flows only be permitted to be taken

into account as additional credit enhancement in the SFA calculation in determining the values of L and the amount of the underlying exposures ("UE") to the extent that:

- the bank has received prior approval from the relevant banking agency to do so. Such approval would be conditioned on the bank's demonstrating that it has a comprehensive understanding of risk characteristics of its individual securitization exposures and the risk characteristics of the pools underlying its securitization exposures;

- the bank can access all relevant performance information on the underlying pools on an on-going basis in a timely manner. For re-securitizations, the bank must have information not only on the underlying securitization tranches, such as the issuer name and credit quality, but also on the characteristics and performance of the pools underlying the securitization tranches;

- the bank has a thorough understanding of all structural features of the relevant securitization transaction that would materially impact the performance of the bank's securitization exposure;

- the cash flow methodology used by the bank is (i) commercially available, (ii) transparent and verifiable and (iii) used by the bank for purposes other than the calculation of risk-based capital requirements, such as risk management or impairment analysis; and

- the additional cash flow credit enhancement for a securitization exposure is based on a projection of the available cash flows for the benefit of such securitization exposure determined by undertaking specific steps that are consistent with industry best practices.

V. THE PROPOSED RRBA

A. The maturity adjustment to the RRBA should be calibrated to the revisions to the maturity adjustment to the MSFA that the ASF proposes in Part III.C. of this letter.

In Part III.C. above, the ASF proposes changes to the maturity adjustment to the MFSA to properly take into account the availability of income on securitized exposures to absorb losses on senior securitization tranches for exposures with maturities of greater than one year. The maturity adjustment to the RRBA should be similarly adjusted to assure consistencies in securitization risk weights as between the MSFA and the RRBA.

B. The requirement that investing banks obtain more than one rating in order to use the RRBA should only apply to new securitizations.

As the Committee recognizes in the Consultative Paper, the requirement for two external ratings in order to use the RRBA could be difficult to implement and costly to banks. As many existing securitizations that banks invest in only have one rating in light of the requirements of existing capital regulation in certain jurisdictions, we request at a minimum that any requirement for two or more ratings not apply to existing securitization transactions in jurisdictions where investing banks would currently be permitted to use the RBA with a single rating.

VI. THE PROPOSED SSFA

A. K_{SSFA} must be revised to be made more sensitive to the credit quality of the relevant securitized assets in order for the SSFA to appropriately correlate with the RRBA.

By using Standardized Approach methodology for calculating K_{SSFA}, the proposed SSFA ignores differences in the credit quality of exposures of the same broad category underlying a securitization position. For example, prime auto loans and sub-prime auto loans are assigned the same risk weight under the general risk-based capital rules. This methodology for calculating K_{SSFA} penalizes banks for investing in higher credit quality transactions with low loss levels and therefore low attachment points. Conversely, the performance of certain "sub-prime" assets was not as strong during the recent crisis. Any adjustment to K_{SSFA} based on credit quality should therefore also include an upward adjustment to K_{SSFA} for these asset types.

Because credit quality differences in underlying asset pools can be taken into account by rating agencies in determining the credit ratings that form the basis of the RRBA and must be taken into account in determining K_{IRB}, which forms the basis of the MSFA capital calculation, it would be difficult to "broadly align" risk weights for identical securitization exposures under the RRBA, MSFA and the SSFA, as the Committee states that intends to do, without making the adjustments to K_{SSFA} (and the adjustment of the value of p as described below). We look forward to discussing with the Committee in a comprehensive way what risk weights and key risk factors would be appropriate to apply for purposes of determining K_{SSFA}.

B. The value of the supervisory multiplier p should be adjusted in order to permit risk weights determined under the SSFA with our proposed modifications to correlate as close as possible with risk weights determined using the MSFA or RRBA with our proposed modifications.

The supervisory multiple p of 1.50 proposed for the SSFA in its current form would result in a significant overstatement of capital for many securitization exposures. While the ASF understands that the supervisory multiple is intended to introduce additional conservatism to risk weights derived using the SSFA, it is equally clear that there is a better, more risk sensitive way to derive the risk weights of securitization exposures under the SSFA than the use of a p of 1.50, which acts as a one-size-fits-all instrument for increasing capital for securitization exposures generally without giving appropriate recognition either to the structural protections that are

already embedded in the SSFA calculation or to the significance that differences in credit quality of the underlying exposures can have on the quality of each related securitization exposure.

The ASF therefore believes that p should be set at whatever level permits the closest correlation possible between risk weights determined under the SSFA with our proposed modifications and risk weights determined using the MSFA or RRBA with our proposed modifications.

C. The delinquency variable *W* in the SSFA should be defined to exclude interest payments that are deferred under the relevant contract for reasons not directly related to the creditworthiness of the underlying obligor.

Under the proposed SSFA, variable *W* would equal the ratio of the amount of any underlying exposures within the securitized pool that were "delinquent" to the ending balance. As currently worded, variable *W* treats a securitized financial asset with a contractually deferred interest payment for 90 days or more as delinquent, regardless of the reason for such deferral. Because contractual interest payments may be deferred by contract for reasons that do not relate to the creditworthiness of the obligor of the financial assets, the ASF believes that variable *W* should be modified to avoid treating as delinquent interest payments that are contractually deferred for reasons other than the deterioration of an obligor's creditworthiness.

Securitizations of both student loans and credit cards and other consumer installment receivables could be significantly adversely affected under the current wording of variable *W*. Student loans are structured to defer a borrower's payments during specified periods based on the borrower's student status.[10] Similarly, credit cards and other consumer installment loans often contain provisions designed to promote sales of consumer products that permit the obligor to defer interest payments on receivables for certain specified time periods.[11] Although neither of these types of deferrals results from a credit issue with respect to the obligor, the Consultative Paper suggests that the loans would be considered "contractually deferred" during these periods and, therefore, such loans would be included in the computation of variable *W* in the SSFA calculation.

Our members believe that variable *W* was not designed to capture the interest deferrals described above and that instead it was intended to capture contractual deferrals of interest that occur due to credit issues with the obligor of the financial asset. Therefore, the ASF suggests that the definition of "delinquent exposures" be modified as follows:

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[10] For example, many student loans (i) do not require payment while the borrower is enrolled in school, (ii) provide a grace period after graduation before payments are required and (iii) provide for deferment of payment obligations upon the borrower's return to school to complete a degree or conduct post-graduate study.

[11] For example, a consumer may agree to buy furniture with no interest for six months. Although interest accrues on the transaction from the date it is executed, no interest is due if the consumer pays the full amount of the receivable within six months. However, if the consumer does not pay the balance within such six-month period, the accrued interest is added to the principal balance of the receivable.

> "… exposures that… had contractually deferred interest payments for 90 days or more ***other than (i) deferred interest payments on FFELP student loans incurred during periods of deferment and/or forbearance, and (ii) interest payments that are deferred as a result of provisions or events set forth in the contract as of its effective date that are not directly related to the creditworthiness of any obligor under the contract***, or…"

Because the U.S. federal government guarantees 97% to 100% of the principal and accrued interest of FFELP student loans, the bank's risk of loss associated with payment deferrals of this nature is 3% or less. In light of this guarantee, the ASF requests that contractual deferrals of interest for 90 days or more with respect to FFELP student loans that occur *for any reason* not be treated as delinquent receivables for purposes of variable *W*. With respect to all other categories of receivables (including private student loans), the ASF is requesting that the exclusion apply only with respect to deferrals resulting for the occurrence of pre-determined events set forth in the contract that are not directly related to the creditworthiness of any obligor on the financial asset. These changes are consistent with what we believe is the purpose of this clause in variable *W*—to capture as delinquencies deferrals offered by a lender as a result of a deterioration in the obligor's creditworthiness.

VII. THE PROPOSED CONCENTRATION RATIOS

A concentration ratio ignores the positive effects of asset overcollateralization that is not in the form of an issued securitization position on the risk inherent on the positions that benefit from the same. It is also insensitive to the risks inherent in the securitized exposures, and therefore does not appropriately distinguish credit risk exposures within asset classes, providing for timely and accurate measurements of credit quality, and fostering prudent risk management. As a result, concentration ratios should only be used to determine the capital requirements for securitization exposures where a more risk sensitive approach is not available, in particular where the information necessary to determine capital under a more risk sensitive approach does not exist.

Using a concentration ratio as the sole approach under Alternative B to determine capital for all securitization exposures that are not "high quality securitization exposures" and using the BCRA for all re-securitizations under both alternatives are inconsistent with the principles set forth above.

VIII. THE DEFINITION AND TREATMENT OF RE-SECURITIZATION EXPOSURES

As discussed above, the requirement that capital for re-securitization exposures may only be determined under the BCRA does not seem warranted. Use of the BCRA assumes in effect that all securitization exposures underlying the re-securitization are alike from a credit quality perspective and that there is no positive effect on the performance of the exposure from the credit enhancement that supports the exposure. These are not accurate assumptions and they can result in both an overstatement of the capital required for a re-securitization exposure, in the case of re-securitization exposures where the underlying securitization exposures are of high credit quality or where credit enhancement supporting the exposure is significant, and an understatement of the capital required for a re-securitization exposure, in the case of re-securitization exposures where the underling securitization exposures are of relatively lower credit quality. Where the information necessary to calculate the risk weight of a re-securitization exposure under the MSFA, RRBA or SSFA is available, a bank therefore should be permitted to determine such risk weight using these approaches.

In the event that the Committee elects not to permit securitization exposures to re-securitizations to use the MSFA, RRBA or SSFA approaches, the definition of "re-securitization" must be narrowed to exclude certain securitization exposures from its scope. The ASF acknowledges that the risks presented by opaque and extraordinarily complex re-securitization exposures were made apparent during the recent financial crisis, and we appreciate the need to treat these exposures more stringently under the revised capital framework. However, we believe that it is important to define "re-securitization" in a manner that does not unduly penalize re-securitization exposures that are straightforward and behave like plain vanilla wholesale exposures.

In defining "re-securitization," we believe that the Committee should emphasize that a re-securitization involves more than one underlying exposure. Re-securitizing a single securitization exposure - which occurs, for example, in a Re-REMIC - is substantively the same as adding credit enhancement to that exposure. It would be incongruous to treat a credit-enhanced re-securitization exposure of a single securitization exposure as more risky than the underlying securitization exposure itself.

Further, we note that collateralized loan securitizations ("CLOs") historically have included a small percentage of other CLO exposures. The inclusion of these underlying CLO exposures has been designed to protect banks and other investors by enhancing diversification and liquidity within the CLO. To our knowledge, this small basket of underlying CLO exposures has never been cited negatively in the performance review of any CLO, which is not surprising in light of their insignificant magnitude, their investor-focused purpose, and their risk being reflective of the rest of the underlying corporate loan exposures. In addition, it would be extremely difficult to amend existing CLO transactions to remove their underlying securitization exposures. We would therefore propose that the definition of re-securitization exclude existing securitization exposures to CLOs where 5% or less of the underlying exposures are securitization exposures. To add conservatism to this exception, the Committee could assign a zero dollar value to each

securitization exposure that underlies a securitization exposure for which this proposed definitional exception would apply.

Further, securitizations of senior securitization exposures that are individually underwritten by the investing bank and to which the bank can and does assign and individual risk-based capital charge should be allowed to use the MFSA, RRBA/IAA and SSFA approaches rather than the BCRA regardless of any other change that the Committee makes to the treatment of re-securitizations under the capital framework. Such transactions share little in common with the transactions we believe give rise to the Committee's concerns with re-securitization exposures generally.

For example, certain securitization exposures to asset-backed commercial paper (ABCP) conduits that banks hold either as investors in the ABCP or as providers of program-wide liquidity or credit enhancement exposures are currently treated as re-securitizations in the Committee's capital guidelines. Multi-seller asset backed commercial paper conduits are an important source of funding receivables such as trade receivables, auto loans and leases, credit card receivables and commercial loans in the broader economy. Determination of capital under the BCRA would ignore the substantial credit enhancement that typically exists for these exposures and would thereby greatly increase the capital that banks would be required to hold against these exposures and would either increase the cost to customers of obtaining financing or discourage banks from participating in the ABCP market. This result would have a significant impact on the availability of financing to businesses and consumers and could therefore have a significant impact on the overall economy.

We believe the Committee should consider excluding securitization exposures to multi-seller ABCP conduits of the type described above and other securitization exposures where each of the underlying exposures is a senior securitization exposure from the definition of re-securitization exposures if the bank sponsoring the ABCP conduit or otherwise investing in the securitization exposure underwrites and approves each exposure under its normal process for approving credit exposures, and, if the exposure is to an ABCP conduit: (1) the ABCP issued by the conduit is of a single class that is not subordinate to any other obligation of the ABCP conduit, (2) each of the credit exposures of the ABCP conduit is individually negotiated with a receivables seller, and (3) the sponsoring bank provides liquidity facilities to the ABCP conduit in an amount that covers at least 100% of the face amount of its ABCP.

IX. THE 1,250 % MAXIMUM RISK WEIGHT

Under the revised framework, a 1,250% risk weight would be assigned to any securitization exposure if none of the other approaches could be used. This would impose a penalty on banks with higher risk-based capital ratios and more robust capital positions. As observed by the U.S. Agencies in the U.S. Advanced Approaches NPR[12], which similarly defaults to a 1,250% risk weight, "[t]he more a risk-based capital ratio exceeds 8.0%, the harsher is the effect of a 1,250% risk weight on risk-based capital ratios. Conversely, the effect of a 1,250% risk weight would be less harsh than a deduction from total capital for any risk-based capital ratio that is below 8.0%." Such an outcome (as well as its related incentives and disincentives), runs counter to other financial-reform initiatives that are driving banks to increase and maintain sizeable cushions of loss-absorbing capital well in excess of 8.0%. We believe that the aim of reducing disparities in the measure of capital for leverage and risk-based capital purposes can be achieved without creating a meaningful disincentive for banks to maintain robust capital positions well above regulatory minimums. As a result, the ASF proposes that a cap on the amount of risk-based capital that a bank must hold for any securitization exposure be fixed at the amount of that exposure (a dollar-for-dollar cap).

X. MAXIMUM CAPITAL CHARGE (OVERALL CAP)

The ASF appreciates that the Committee is applying a limitation on the maximum capital charge for originators and sponsors using the Standardized Approach securitization framework at the capital requirement that would apply if the securitized exposures were held directly by the bank. We believe that this limitation should be extended to include banks using the Standardized Approach that are investing in securitizations. The principle set forth in the Consultative Paper that the process of securitization should not result in more capital being held after a securitization than before applies equally to a situation where a bank invests in a securitization transaction in which it does not originate the assets.

The ASF also requests that the Standardized Approach cap described above clearly be made available to Advanced Banks using the RRBA or the SSFA that invest in securitization exposures and that do not have the information necessary to determine the risk weights of the underlying assets under the IRB approach. Applying such a cap would promote a consistency in capital outcomes as between Advanced Approaches banks and Standardized Approach banks.

XI. MAXIMUM RISK WEIGHT FOR SENIOR SECURITIZATION EXPOSURES

Similar to our request above with respect to the overall cap, the ASF requests that the Standardized Approach risk weight cap for senior exposures clearly be made available to Advanced Banks using the RRBA or the SSFA that invest in securitization exposures and that do

[12] *See* Agencies, "Regulatory Capital Rules: Advanced Approaches Risk-Based Capital Rules; Market Risk Capital Rule," 77 Fed. Reg. 52, 978 (Aug. 30, 2012) (the "U.S. Advanced Approaches NPR" and the rules set forth therein the "Advanced Approaches").

not have the information necessary to determine the risk weights of the underlying assets under the IRB approach. Applying such a cap would promote a consistency in capital outcomes as between Advanced Approaches banks and Standardized Approach banks.

XII. EARLY AMORTIZATION PROVISIONS

In the Consultative Paper, the Committee proposes to require an originator or seller into a securitization of revolving credit exposures that incorporates an early amortization provision to assess all of the securitized assets as if they were "on-balance sheet" for regulatory capital purposes. Securitizations of revolving assets are an important financing and risk management tool for banks and the presence of early amortization provisions is an important structural element of these transactions. The proposal is based on the Committee's perception that securitizations with early amortization provisions do not achieve a significant transfer of risk because the credit risk sometimes reverts back to the originator, either when the early amortization provisions are triggered or when the originator takes steps to avoid the triggering of the early amortization. Our members believe, however, that the negative consequences associated with the trigger of an early amortization are substantial and serve as a sufficient deterrent to mitigate the Committee's concern. More specifically, (i) actions taken to avoid the occurrence of an early amortization could have significant accounting and regulatory capital implications in jurisdictions (such as Canada) in which originators enjoy off-balance sheet treatment for securitized assets, and (ii) the occurrence of an early amortization would damage the originator's reputation and ability to market other securitizations. Furthermore, a bank's supervisory authority should have other tools available to it to address any concerns that a bank may implicitly support a revolving securitization transaction when it is not legally obligated to do so.[13]

XIII. TREATMENT OF WRITE-DOWNS AND PURCHASE DISCOUNTS

In the Consultative Paper, the Committee proposes that write-downs and discounts be addressed in the securitization framework by using the carrying value as the amount to be risk weighted, rather than the notional value. The ASF agrees with this proposal. Carrying value is an exceedingly important factor in the amount of risk-based capital a bank must hold against a security. Specifically, a notable discount to par for a particular position is typically indicative of a security that has either been previously written-down (e.g., through Other Than Temporary impairment) or a security that has been purchased in the secondary market, where the markets are highly proficient at pricing risk. The discount to par for a particular position provides additional protection to the holding value of the position than the same security being held at a discount to par. As such, carrying value must be included in the calculation of risk-based capital.

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[13] For example, if the Board of Directors of the U.S. Federal Deposit Insurance Corporation ("FDIC") determines that a bank under its jurisdiction is engaging in the "unsafe or unsound practice" of operating with an inadequate level of capital for the kind or quality of assets held and the bank fails to take the corrective action prescribed by the FDIC, the FDIC could exercise its broad enforcement powers to terminate insurance or issue a cease and desist action.

The MSFA should also take into account any positive difference between the par value and carrying value of a securitization exposure as additional credit enhancement ("L") for purposes of the MSFA calculation. Such carrying value differential provides additional protection to the holder of a securitization position. Because losses on the underlying assets would be absorbed by this difference before the bank would take further write downs (losses) on its position, it needs to be included in L for that term to reflect all credit enhancement. The ASF notes in this regard that the Committee includes in L the discount in the purchase price for the underlying securitized receivables. Since the two discounts have the same economic effect, the ASF sees no basis for distinguishing between the two discounts in computing L. A corresponding adjustment should also be made to the thickness of the relevant position ("T"). Similarly, any positive difference between the par value and the carrying value of a securitization should also be taken into account as additional credit enhancement in determining the attachment point ("A") of a securitization exposure in calculating the SSFA.

The ASF very much appreciates the opportunity to comment on the Consultative Paper. Should you have any questions or desire any clarification concerning the matters addressed in this letter, please do not hesitate to contact me at 212.412.7107 or at tdeutsch@americansecuritization.com.

Sincerely,

Tom Deutsch

Tom Deutsch
Executive Director
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