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Via Email: gdsr@iosco.org

Mr. Tim Pinkowski
General Secretariat
International Organization of Securities Commissions (IOSCO)
Calle Oquendo 12
28006 Madrid
SPAIN

Re: *Public Comment on Global Developments in Securitization Regulation*

The American Securitization Forum ("ASF")[1] appreciates the opportunity to submit this letter in response to the consultation report (the "Consultation Report") entitled "Global Developments in Securitization Regulation" published by the International Organisation of Securities Commissions ("IOSCO") in June 2012.[2] ASF serves to provide securitization industry consensus on market and regulatory issues, and we have established an extensive track record of providing meaningful comment to various regulatory agencies and IOSCO on issues affecting our market. Our views as expressed in this letter are based on feedback received from our broad membership.

I. Introduction

A. Consultation Background

The Consultation Report is part of a larger effort by the Financial Stability Board ("FSB"), acting upon the request of the G20, to develop recommendations to strengthen oversight and regulation of the securitization sector.

As set out in more detail in the Consultation Report, the FSB's Standing Committee on Supervisory and Regulatory Cooperation ("FSB SRC") requested IOSCO to conduct a stock-taking exercise in relation to regulations for risk retention and measures promoting the standardization of disclosure procedures as well as a higher degree of transparency in the securitization market. As a result, IOSCO's Task Force on Unregulated Markets and Products ("TFUMP") was asked to undertake a project which describes and analyzes global regulatory and industry initiatives on risk retention, transparency and disclosure standardization, identifies

[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 330 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.iosco.org/library/pubdocs/pdf/IOSCOPD382.pdf.

and assesses material differences in regulatory and industry approaches, and recommends, where appropriate, approaches to addressing identified material differences.

In this context, it was noted that a confidential preliminary analysis (the "SEC/EC Staff Report") conducted by the staff of the Securities and Exchange Commission ("SEC") and the European Commission ("EC") found differences in approaches to the aforementioned regulatory initiatives which may impact securitizations, especially in cross-border transactions.[3] The SEC/EC Staff Report, however, concluded that these differences did not amount to "material incompatibilities." In contrast, the Joint Forum, in a report published in July 2011, also noted the differences in approach between the U.S. and Europe but highlighted the importance of consistent and aligned approaches in developing a regulatory framework for securitization. The Joint Forum urged authorities to strive for consistency across global markets and sectors and to resolve uncertainties in a timely manner.

As the FSB SRC's request to IOSCO indicated, securitization is a valuable funding technique and an efficient means of diversifying risk. Specifically, securitization helps support economic recovery by offering an investment opportunity for investors and an alternative source of funding for entities originating credit for the real economy. This in turn enables originators to increase the amount and diversity of types of financing available to the economy, matches investors seeking high-quality assets with originators seeking liquidity, and encourages overall economic growth. Because our financial system is global, however, securitization, to be effective, needs to be able to operate smoothly across borders – to provide the maximum benefits, originators of credit for consumers and businesses need to be able to finance these assets as efficiently as possible, by offering securities backed by these assets to the broadest range of appropriate investors possible, not just those located in their home jurisdiction. Likewise, investors, such as insurance companies, pension funds and money managers, should be able to select from the widest range of investments relevant to them. With banking institutions increasingly constrained in the amount and type of credit they can supply, the ability of these other investors to provide an alternative sourcing of financing for consumers and businesses depends on unimpeded cross-border capital markets. Disparate regulatory schemes between jurisdictions that hinder or prevent cross-border securitization activity, negatively impacting economic activity without any significant offsetting policy benefits, merit a strong policy response.

While the policy intent of regulatory requirements relating to securitization and asset-backed securities ("ABS") in both the U.S. and Europe is similar, the many differences between proposed and recently adopted requirements in the two regulatory regimes create significant "frictions" resulting in the preclusion of certain transaction types, increased costs of compliance, and loss of flexibility, particularly in the area of cross-border securitization, directly constraining the amount of credit available to consumers and businesses in the real economy. In order to support the recovery of securitization markets, ASF strongly supports initiatives to align regulatory approaches, where practicable and beneficial. This response letter highlights the most

[3] THE BOARD OF THE INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS, *Global Developments in Securitization Regulation*, CR09/12, June 2012, p. 2 (internal quotations omitted).

important frictions between regulatory requirements across jurisdictions and recommends policy approaches to minimize their impact on cross-border securitization.[4]

B. Regulatory Background

i. United States

In the United States, the main initiative for the regulation of securitization undertaken by legislators has been the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank"), of which Section 941(b) was codified as Section 15G of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Section 15G aims to align the interests of investors and originators and to ensure the quality of the securitized assets. Furthermore, Section 942(a) of Dodd-Frank provides for specific disclosure standardization requirements. In April 2011, a notice of proposed rulemaking entitled "Credit Risk Retention" (the "U.S. Credit Risk Retention Proposal")[5] was released by the Federal Deposit Insurance Corporation, the Federal Reserve Board of Governors, the Office of the Comptroller of the Currency, the SEC and, with respect to the securitization of residential mortgage assets, the Federal Housing Finance Agency and the Department of Housing and Urban Development (the "Joint Regulators"). While we recognize that this proposal is subject to change when adopted in final form, our analysis in this response letter is based on the U.S. Credit Risk Retention Proposal in its current form. ASF submitted a response letter on June 10, 2011 to the Joint Regulators in regard to the U.S. credit risk retention proposed regulations ("ASF Response Letter").[6]

In 2010, shortly before the passage of Dodd-Frank, the SEC released a proposal to update Regulation AB (the "Reg AB II Proposal"), which contained new, wider and more specific rules concerning disclosure requirements for ABS sold in the U.S. In response to the Reg AB II Proposal, ASF assembled an unprecedented industry-wide representative taskforce that submitted extensive comments to the SEC.[7] Specifically, ASF submitted a broad, 172-page primary comment letter on August 2, 2010 detailing our members' views relating to the majority

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[4] A separate but related "friction" for securitization has recently arisen under the commodity pool operator regulations adopted by the U.S. Commodity Futures Trading Commission (the "CFTC"). These regulations, which result from the melding of existing commodities regulation with new swaps regulation, may lead to outcomes that impose significant burdens on securitization market participants without advancing the goals of Dodd-Frank. This is a particular concern for ASF in the context of securitization vehicles that make limited use of swaps for hedging purposes. ASF is concerned that many such vehicles may find themselves classified as commodity pools after the effective date of changes in law that bring swaps within the definition of commodity pool, even when they do not satisfy key aspects of the criteria for commodity pools. ASF is also concerned that many securitization vehicles, including those that will not enter into additional swaps following their formation, are structured in a way that will make compliance with commodity pool operator regulations difficult or impossible. If enforced as currently in place, non-U.S. securitizers seeking to access the U.S. investor base could inadvertently find themselves required to register with the CFTC as "commodity pool operators," further discouraging cross-border activity.

[5] *See* http://edocket.access.gpo.gov/2011/pdf/2011-8364.pdf.

[6] *See* http://www.americansecuritization.com/uploadedFiles/ASF_Risk_Retention_Comment_Letter.pdf.

[7] For more information about ASF's Reg AB II response, *see* http://www.americansecuritization.com/index.aspx?id=4410.

of the disclosure and reporting proposals set forth in the Reg AB II Proposal, including specific responses to the RMBS and credit and charge card disclosure regime proposals.[8] On that same day, ASF submitted a supplemental comment letter focusing solely on issues relating to asset-backed commercial paper ("ABCP"), including disclosure and reporting requirements tailored to that market.[9] Additionally, following these submissions, ASF submitted, among other materials, a supplemental comment letter dedicated solely to addressing disclosure issues relating to assets underlying auto loan, auto lease and auto floorplan ABS.[10]

On August 5, 2011, the SEC published in the *Federal Register* revised proposals of certain provisions that were initially proposed in the Reg AB II Proposal (the "Reg AB II Re-Proposal"),[11] in light of, among other things, several provisions enacted as part of Dodd-Frank. On October 4, 2011, ASF submitted our primary comment letter in response to the Reg AB II Re-Proposal.[12] Additionally, ASF member issuers of, and investors in, equipment ABS submitted a thorough supplementary comment letter dedicated solely to addressing disclosure issues relating to assets underlying equipment loan and lease ABS (the "ASF Reg AB II Equipment Disclosure Comment Letter").[13]

ii. Europe

European regulations and proposals have so far been addressed to credit institutions and insurers, respectively, as investors or parties that take exposure to securitizations, rather than being addressed to sponsors and originators of ABS, as most existing and proposed regulations in the United States are drafted. In this letter, we refer to such European entities that take exposure to securitizations as "European Regulated Investors."

The primary response in Europe for regulating the exposure of credit institutions to securitizations is the Directive 2006/48/EC (Capital Requirements Directive ("CRD")), updated by the Directive 2009/111/EC of September 16, 2009. The CRD provides in Article 122a for a specific and detailed regulation of risk retention, transparency and disclosure standardization requirements (see below).

In addition to the CRD, the European Commission has also introduced specific regulation with regard to insurance companies, namely the Directive 2009/138/EC ("Solvency II"), which provides for detailed requirements for transparency and disclosure standardization, as well as further capital-related requirements with respect to securitization exposures. Solvency II, however, has not come into effect yet, though is scheduled to do so on January 1, 2014.

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[8] *See* http://www.americansecuritization.com/uploadedFiles/ASFRegABIICommentLetter8.2.10.pdf.

[9] See http://www.americansecuritization.com/uploadedFiles/ASFRegABIIABCPCommentLetter8.2.10.pdf.

[10] *See* http://www.americansecuritization.com/uploadedfiles/asf_reg_ab_ii_auto_abs_comment_letter_8.31.10.pdf.

[11] *See* http://www.gpo.gov/fdsys/pkg/FR-2011-08-05/pdf/2011-19300.pdf.

[12] *See* http://www.americansecuritization.com/uploadedFiles/ASF_Comment_Letter_on_SEC_Reg_AB_II_Re-Proposal_10-4-11.pdf.

[13] *See* http://www.americansecuritization.com/uploadedFiles/ASF_Equipment_ABS_Letter_(11-2-11).pdf.

Beyond the European legislative regulatory approaches, various institutions have brought forward non-legislative regulatory initiatives. The European Central Bank ("ECB") has introduced disclosure requirements for ABS eligible under the Eurosystem collateral framework. Similarly, but more comprehensively, the Bank of England has introduced disclosure templates as well as requirements concerning transaction transparency and investor information. In this respect, trade associations have promoted a "comply or explain" policy regarding the implementations by the Bank of England.

II. Risk Retention

Although E.U. and U.S. risk retention rules have similar objectives, the policy approaches taken by the regulators in the respective jurisdictions are materially different, which will cause significant transactional frictions in cross-border securitizations. As noted in the IOSCO Report, the U.S. risk retention proposals are addressed to all "securitizers,"[14] in contrast to European regulations, which, as discussed above, regulate the investment activities of credit institutions and propose to regulate those of insurers. The result of this discrepancy in approaches, if implemented as currently proposed, is that a U.S. securitizer seeking to sell ABS to European Regulated Investors will be obliged to comply with the risk retention requirements in both jurisdictions. Similarly, European transactions that do not fall within the very limited safe-harbors available in the U.S. Credit Risk Retention Proposal would be potentially subject to two levels of risk retention regulation. Issuers outside of both jurisdictions with any own home country retention requirements may then be required to comply with three (or more) sets of retention rules.

While certain transactions would need to be restructured to comply with both sets of regulations, others will be effectively precluded entirely, rendering the global market for ABS appreciably less efficient.[15] To the extent securitizers are able to, and opt to, comply with both sets of regulations, the additional costs of compliance will be borne in the first instance by securitizers and ABS investors, but ultimately the costs will be borne by consumers and businesses to the detriment of the larger real economy. Even where an immediate increased compliance cost is difficult to identify, discrepancies in regulations will result in a loss of the very flexibility that promotes the innovative and efficient functioning of the securitization markets in a highly dynamic economic environment. These are the three consequences of disparate regulation – hindrance or preclusion of certain transactions, increased regulatory compliance costs, and a loss of structural flexibility – that are most clearly manifest, but there are

[14] The term "securitizers" includes "(A) an issuer of an asset-backed security; or (B) a person who organizes and initiates an asset-backed securities transaction by selling or transferring assets, either directly or indirectly, including through an affiliate, to the issuer."

[15] One feature contained in the U.S. Credit Risk Retention Proposal (without a European equivalent) is the premium capture cash reserve account. ASF strongly believes that, if adopted in the U.S., this proposal would create severe frictions in the global ABS marketplace. As noted in the ASF Response Letter (as defined below), the premium capture cash reserve account will have a series of adverse effects, including disincentives to securitize, increased cost of capital through accounting consolidation, lack of access to quality of assets, and negative pressure on home values. Non-U.S. issuers would be reluctant to sell into the U.S. beyond the safe harbor made available by the U.S. Credit Risk Retention Proposal, if as a consequence such issuers would be subject to the U.S. premium capture rules.

undoubtedly other consequences that will come to light as practitioners endeavor to comply with incongruous regulations in force in different jurisdictions in the context of actual transactions.[16]

A. Retention Mechanisms

The U.S. Credit Risk Retention Proposal identifies several credit risk retention mechanisms, including vertical, horizontal, retention by a sponsor of a representative sample and several asset-specific types of retention. Article 122a, on the other hand, adopts a more simplified approach and provides only extremely limited asset-specific types of retention. The discussion below highlights areas where cross-border application of the disparate existing and proposed risk retention mechanisms in the U.S. and Europe would hinder or possibly preclude cross-border offerings of ABS.

i. ABCP Programs

Under the U.S. Credit Risk Retention Proposal, subject to extensive conditions, the sponsor of an "eligible" asset-backed commercial paper conduit ("ABCP Conduit") will be permitted to satisfy its base risk retention obligations if each originator-seller that transfers assets to collateralize the securities issued by the ABCP Conduit retains the same amount and type of credit risk as would be required under the horizontal risk retention option if the originator-seller was the sponsor of the intermediate special purpose vehicle. We have outlined our criticisms of this approach in ASF's Follow-Up ABCP Risk Retention comment letter addressed to the Joint Regulators, dated February 23, 2012.[17]

Alternatively, according to guidelines (the "CEBS Guidelines") issued by the Committee of European Banking Supervisors ("CEBS"), a European sponsor of an ABCP Conduit will be able to fulfill its risk retention obligations under Article 122a by either providing a liquidity facility to its ABCP Conduit that ranks senior to other obligations in the waterfall and covers 100% of the credit risk of the underlying exposures (risk retention option "a)" of Article 122a) or by providing for a stand-by letter of credit of an appropriate amount as program-wide credit enhancement for the ABCP Conduit.

Currently in Europe, ABCP is subject to a grandfathering clause that exempts compliance with Article 122a until December 31, 2014 by any ABCP Conduit that issued ABCP prior to January 1, 2011. Depending on when the U.S. Credit Risk Retention Proposal becomes effective, frictions would arise between the time of its adoption in the U.S. and the conclusion of the European grandfathering period as a result of European ABCP Conduits being required to comply with sponsor-level credit risk retention in the extremely prescriptive manner mandated in

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[16] We note for IOSCO's consideration that there may be a range of unintended consequences to disparate regulation of securitization between the U.S. and Europe. For example, European investors may seek access to "qualified residential mortgage" assets (see discussion in II. B.) via synthetic structures, or may take other structural steps to achieve the economic effect of a transaction rendered unworkable due to some of the transactional frictions identified herein. These market responses may render the market for securitization less stable, and the balance sheets of large institutional holders of ABS more volatile, with corresponding impacts to the real economy.

[17] *See* http://www.americansecuritization.com/uploadedFiles/ASF_ABCP_Risk_Retention_Follow_Up_2_23_12.pdf.

the U.S. Once both regulatory regimes are in place, the transactional frictions of complying with both forms of risk retention will likely cause sponsors of ABCP Conduits to have to significantly restructure their vehicles, inevitably increasing expense and complexity with no offsetting regulatory benefit. Sponsors may even abandon cross-border issuance altogether. Given the importance of access to dollar funding in the U.S. capital markets for European sponsors of ABCP Conduits, these transactional frictions could prove particularly onerous to them.

ii. Managed CLOs

Under the U.S. Credit Risk Retention Proposal, the current view is that managers of collateralized loan obligations ("CLOs") will generally be considered "sponsors" of the securitization and will therefore be obliged to comply with the risk retention requirements applicable to ABS securitizers. In Europe, more flexibility is afforded to managed CLOs. Credit risk may be retained in certain circumstances by an anchor investor (rather than the CLO manager). Applying the prescriptive approach proposed in the U.S. would create a friction for managed CLO offerings from Europe into the U.S. where the manager is not sufficiently capitalized to retain the credit risk but there are other indicia of appropriate transaction discipline supporting the policies behind risk retention (such as a third-party anchor investor acquiring and holding an appropriately sized junior interest). This would have some preclusive effects, and ultimately would reflect a diminishment of flexibility for cross-border managed CLO offerings.[18]

iii. CMBS "B-Piece" Buyers

The U.S. Credit Risk Retention Proposal and European regulations apply different approaches to offerings of commercial mortgage-backed securities ("CMBS"). The proposed U.S. rules permit an originator of CMBS to meet its risk retention requirements by having a third party ("B-piece buyer") acquire an eligible horizontal residual interest in the issuing entity that, in addition to satisfying other conditions, complies with the risk retention rules that would have been applicable to the originator.[19] The European regime has not been clear as to whether the involvement of a B-piece buyer would comply with the risk retention requirements of Article 122a (or what conditions would apply to such involvement, if so). According to the CEBS Guidelines, it can be sufficient that a B-piece buyer complies with the risk retention provisions given that the buyer was sufficiently involved in the selection of exposures and the structuring of tranches in a CMBS transaction and that he had an aligned interest with the originator; however, there remains uncertainty as to how to apply this in practice. ASF is in favor of harmonizing the approach to CMBS issuances between the two jurisdictions, particularly where lack of such harmony may preclude cross-border CMBS transactions structured with a B-piece buyer.

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[18] *See* page 133 of the ASF Response Letter for a more detailed discussion of CLOs *at* http://www.americansecuritization.com/uploadedFiles/ASF_Risk_Retention_Comment_Letter.pdf.

[19] Such conditions include the B-piece buyer having to hold the retention for the duration of the transaction and disclosing the purchase price paid. These conditions would severely limit the attractiveness of such an investment, and drive up desired yields to invest.

iv. Master Trusts

In the U.S., securitizers of revolving assets (such as credit card receivables) may rely on proposals that would permit securitizers to satisfy their risk retention obligations by holding seller interests in master trusts used to securitize those assets. However, under the U.S. Credit Risk Retention Proposal, this option would be unavailable for residential mortgage-backed security ("RMBS") securitizers, which frequently use the master trust structure for non-revolving assets. This structure is particularly prevalent in the U.K., where master trusts are the dominant means of securitizing residential mortgages. If this approach were to be put into effect, it would represent a significant loss of flexibility, which may preclude U.K. offerings of RMBS into the U.S. capital markets.

v. "L-Shaped" Retention

U.S. issuers seeking to rely on "L-shaped" risk retention, which is one of the credit risk retention options proposed to be made available in the U.S. by the U.S. Credit Risk Retention Proposal (and not similarly available in Europe), will not be able to access European capital markets without either selecting alternative risk retention types that will comply with Article 122a or incurring the cost of additional risk retention on their balance sheets to make up for the shortfall accounted for by the vertical portion of the L-shaped retention.[20] Given the costs of retention, and the possible risks associated with adverse accounting treatment,[21] most securitizers for whom L-shaped retention would be the most viable retention alternative would be obliged to adopt one of the alternative risk retention types. Although ASF expects that L-shaped retention will be used on a limited basis, the Joint Regulators considered its availability sufficiently important to include in the U.S. Credit Risk Retention Proposal.

B. Qualified Residential Mortgages

Section 15G of the Exchange Act exempts from the risk retention requirements ABS collateralized by "qualified residential mortgages" as proposed to be defined in the U.S. Credit Risk Retention Proposal ("QRMs"). Although this definition has not been finalized yet,[22] at the direction of Dodd-Frank, QRM will generally refer to high quality assets with generally lower rates of default than non-QRM assets. European Regulated Investors will be precluded from purchasing ABS supported by QRMs and other assets for which risk retention in the U.S. is not required, resulting in a lower degree of price discovery, decreased liquidity, and consequent potential price distortion in ABS backed by these assets. Contrary to the objectives of European regulators, because of the unavailability of QRM-collateralized ABS to European Regulated

[20] Since the horizontal portion of the risk retention must constitute 2.564% of the par value of the ABS interests in the issuing entity, most issuers would face the decision between foregoing L-shaped risk retention or retaining an additional 2.436% horizontal interest.

[21] Accountants have raised the concern that the retention of a security interest coupled with control through servicer arrangements may preclude sale treatment for the assets.

[22] Section 15G of the Exchange Act directs the Joint Regulators to define jointly what constitutes a QRM, "taking into consideration underwriting and product features that historical loan performance data indicate result in a lower risk of default."

Investors, such investors would have to turn to alternative U.S. ABS investments that may be less safe or more expensive on a risk-adjusted basis in order to take exposure to the U.S. residential mortgage market. Similarly, to the extent that, in the future, European or other regulators develop parallel provisions for ABS backed by local assets deemed of sufficiently high quality that risk retention is not necessary, absent further regulatory action, U.S. investors would be precluded from participating in any such transaction that does not satisfy the cross-border safe harbor provided for in the U.S. Credit Risk Retention Proposal.

C. "Passporting" Approaches to Cross-Border Regulation

In the ASF Response Letter, we proposed creating a limited exemption from the U.S. Credit Risk Retention Proposal for U.S. sponsors of ABS issued in an offering conducted exclusively pursuant to Regulation S of the Securities Act of 1933 (a "Reg. S Only Offering"), so long as at least 10% of the offering is made to investors located in a jurisdiction that maintains substantially similar risk retention requirements to those of the U.S. (a "Qualified Non-U.S. Jurisdiction"). Generally, we will refer to this exemption concept as "Passporting". We requested that the Joint Regulators provide a definition of the term "Qualified Non-U.S. Jurisdiction" in the revised rules. We noted that the definition could refer to a jurisdiction that has implemented, and which maintains, a system of risk retention broadly similar to that found in the U.S. To avoid the need for time-consuming subsequent regulatory action, we further proposed that the definition could specify certain elements of a broadly similar risk retention regime, which, if present, would automatically bring a given non-U.S. jurisdiction within the scope of the new definition.

We also proposed that the Joint Regulators, as part of the issuance of the final version of the U.S. Credit Risk Retention Proposal (possibly in the preamble), make an affirmative determination that Article 122a, in its current form, contains elements that make it broadly similar to the U.S. retention regime, and that, therefore, member states of the European Union that have implemented Article 122a are considered "Qualified Non-U.S. Jurisdictions" for the purposes of the finalized U.S. risk retention rules.[23] Considering that Article 122a, like the U.S. Credit Risk Retention Proposal, aims to align the interests between securitizers and purchasers of securities, and that some of its fundamental requirements are substantially similar to those of the U.S. Credit Risk Retention Proposal (*i.e.*, the base 5% risk retention requirement, the prohibition on certain types of hedging that would defeat the purpose of the retention requirement, etc.), such a determination would greatly assist cross-border securitization offerings, without compromising the Joint Regulators' policy goals.

[23] In the ASF Response Letter, we noted that the current position of the Joint Regulators is that the decision-making process on matters of interpretation and implementation be handled jointly by all relevant Joint Regulators. To the extent that it is agreed that one regulator would have exclusive/special decision-making powers with respect to certain aspects of the risk retention regulations, the Joint Regulators may consider authorizing such regulator to review, from time to time, changes in Article 122a or new risk retention regimes that other jurisdictions may adopt subsequent to the adoption of the finalized risk retention rules. Such reviews could be done, for example, to determine whether Article 122a continues to meet the standards set out in the definition of a Qualified Non-U.S. Jurisdiction or whether other countries' retention regimes that may be adopted following the finalized rules meet those standards.

The exemption we proposed for Reg S Only Offerings would assist in cross border activity for ABS originated in the U.S. and marketed in Europe. To aid in facilitating cross border activity by securitizers based in Europe desiring to sell ABS to investors based in the U.S., we take a different approach. The U.S. Credit Risk Retention Proposal already contains an exemption for non-U.S. issuers selling not more than 10% of the dollar value of proceeds of all ABS interests to or for the benefit of U.S. investors (and meeting certain other conditions) (the "Cross-Border Safe Harbor"). While the threshold provided in the Cross-Border Safe Harbor provides a valuable benchmark for determining when an issuance of non-U.S. ABS has only a slight impact on U.S. markets (and thus does not require application of U.S. risk retention requirements), no distinction was made in the U.S. Credit Risk Retention Proposal between issuances of securities into the U.S. in which the securitizer has conducted no risk retention and issuances in which the securitizer is in compliance with a non-U.S. risk retention regime (such as Article 122a).

We accordingly believe that the 10% cap in the Cross-Border Safe Harbor has a disproportionate effect on non-U.S. issuers that already have expended resources on risk retention and healthy securitization practices. Where a securitizer has already conducted risk retention under regulations in force in a Qualified Non-U.S. Jurisdiction (as defined above), the ABS issued by such a securitizer would be broadly equivalent to ABS issued by a U.S. issuer in compliance with the U.S. Credit Risk Retention Proposal. We therefore believe that it would be appropriate to encourage non-U.S. securitizers to engage in risk retention before issuing into the U.S. by providing them with greater access to U.S. capital markets if they do so.

Accordingly, we propose the provision of a safe harbor in the U.S. for non-U.S. securitizers that have already conducted risk retention in accordance with the rules of a Qualified Non-U.S. Jurisdiction, irrespective of the amount of their U.S. offering. Such a safe harbor would not only ensure an alignment of interests between securitizers and purchasers of securitized assets that should be satisfactory to the U.S. regulators, but it would also be a straightforward and efficient means of addressing inconsistencies among risk retention regimes and thus facilitating cross-border transactions. Specifically, we suggest that IOSCO recommend that the Cross-Border Safe Harbor in the U.S. Credit Risk Retention Proposal be expanded to allow an exemption from compliance with the U.S. Credit Risk Retention Proposal for securitization transactions (i) which comply with the risk retention regime of one or more Qualified Non-U.S. Jurisdictions and (ii) where the offering document used to offer the securities in the U.S. contains an affirmative undertaking by the relevant sponsor(s) or originator(s) to retain a net economic interest in accordance with the risk retention regime of the relevant Qualified Non-U.S. Jurisdiction.

ASF includes below for IOSCO's consideration several additional policy proposals, which are extensions of the Passporting approach initially proposed in the ASF Response Letter and outlined above, to address the frictions identified in this letter.

Our first proposal is for European regulators to consider adopting a Passporting approach similar to that outlined in the ASF Response Letter. That is, if a European Regulated Investor opts to purchase ABS sponsored by a securitizer located in the U.S. and that is subject to and compliant with U.S. risk retention regulations (once adopted and in force), such investor should

be permitted to make the investment without a penalty capital charge. As noted by IOSCO in the Consultation Report, notwithstanding the important technical differences between U.S. and European regulations identified in this letter, the fundamental policies behind the risk retention rules are similar across the jurisdictions. Accordingly, a Passporting approach would facilitate cross-border transactions without sacrificing the broader policy goals of risk retention.

ASF recognizes that Passporting might not be suitable in all circumstances. For example, domestic policy considerations might inform the credit risk retention rules in some jurisdictions, resulting in a regulatory regime that does not accomplish all of the objectives of an investor's applicable regulators. In the U.S., the Joint Regulators propose to privilege certain assets (*e.g.*, QRMs) and designate such assets as not requiring risk retention in order to be securitized. ASF recognizes that, for example, European regulators might disagree with the judgment of the Joint Regulators as to the relative safety of QRM assets or the criteria for determining QRM eligibility, or might not share the policy objectives of the Joint Regulators. In such instances, ASF believes it would nevertheless be appropriate for European regulators to permit a limited level of Passporting, perhaps placing a limitation on what portion of the total portfolio a European Regulated Investor can constitute such assets. The alternative is to *de facto* bar European Regulated Investors from purchasing ABS backed by high quality U.S.-originated residential mortgage assets that qualify for QRM treatment to the detriment of sponsors, U.S. borrowers and European Regulated Investors alike.

Similarly, regulations across jurisdictions should grant relief to securitizers of foreign government-sponsored or guaranteed assets, such as ABS backed by U.S. government guaranteed FFELP student loans in the case of European regulations, or ABS backed by governments or instrumentalities of E.U. member states, in the case of U.S. regulations. Any alternative approach would render such assets less liquid and potentially more volatile. In the ASF Response Letter, we noted that "by providing exemptions to certain U.S. government-backed ABS but not comparable non-U.S. government-backed ABS, the regulators deprive U.S. investors of valuable investment opportunities where the credit worthiness of those instruments is comparable to or greater than certain exempt U.S. government-backed securities, which appear to be exempt for no other reason than national sovereignty."[24] Regulators in both jurisdictions should consider coordinating their regulation of government-sponsored or guaranteed assets to ensure that investors can obtain access to these assets in cross-border transactions, and that the international markets for these assets remain liquid.

III. <u>Transparency</u>

ASF strongly supports the principle that investors in ABS should have access to robust information regarding the cash flows of the asset pools which underlie securitizations in order for investors to make informed investment decisions and to avoid over-reliance on credit rating agencies. However, ASF is concerned about potential discrepancies between the stress testing

[24] *See* page 31 of the ASF Response Letter *at* http://www.americansecuritization.com/uploadedFiles/ASF_Risk_Retention_Comment_Letter.pdf.

requirements in the E.U. and the U.S. We identify below the main differences in stress testing approaches between these two jurisdictions and describe the effect these differences may have.

A. Stress testing information in the E.U.

Article 122a(7) of the CRD provides that sponsors, originators, or original lenders, as the case may be, must disclose to investors, among other things, the information that is necessary for them to perform "comprehensive and well informed stress tests" both on the cash flows of the securitization and on the collateral values supporting its underlying exposures. In the CEBS Guidelines, the CEBS stated that market practice, as opposed to legislation, should dictate the manner by which Article 122a is implemented. Consequently, the CEBS has not suggested that securitizers must develop or obtain a computer software program to generate stress test disclosures. By the same token, the CEBS Guidelines do not provide specific definitions as to what stress testing information means or implies. Issuers currently provide European Regulated Investors with "loan-level" data for ABS backed by residential mortgages and certain other asset classes. Uncertainty remains, however, as to whether in securitizations backed by highly granular assets (*e.g.*, credit cards and auto loans) Article 122a will require loan-by-loan data. One view of the CEBS Guidelines is that they do not require loan-by-loan data for such assets. Any loan-by-loan data provided will use standardized industry templates (such as Bank of England or ECB templates).

ASF strongly believes that the "deference to the market" principle reflected in the CEBS Guidelines should be maintained and that E.U. regulators should consider the comments provided in our various comment letters on the subject before proposing in the future that predictive models be provided to investors.

B. Stress testing information in the United States

In the U.S., Regulation AB requires that originators provide to investors, in connection with the cash flow waterfall, a description of distribution mechanics. Regulation AB does not currently require issuers to provide stress testing models. The cash flow and waterfall information that must be provided is descriptive and can be mapped back to operative transaction agreements governing the cash flow waterfall.

The Reg AB II Proposal, however, would require that most ABS issuers file a computer program with the SEC, in the form of downloadable source code in the Python programming language that gives effect to the flow of funds, or "waterfall," provisions of each ABS transaction. The computer program would have to (i) give effect to the priority of payment provisions in the transaction agreements; (ii) provide the user with the ability to programmatically input (A) the user's own assumptions regarding the future performance and cash flows from the pool assets, and (B) the current state and performance of the pool assets by uploading the proposed asset-level data file that is to be filed at the time of the offering and on a periodic basis thereafter; and (iii) produces a programmatic output, in machine-readable form, of all resulting cash flows associated with the ABS, including the amount and timing of principal and interest payments payable or distributable to a holder of each class of securities. While our issuer and investor members disagreed in their views on the waterfall program, they both agreed

that the SEC's proposal was particularly unclear. Based on the Reg AB II Proposal, it is difficult to determine exactly what was intended by the SEC, and the level of sophistication required in the program. The views of our issuer and investor members on the subject are set forth in the ASF's August 31, 2010 Waterfall Comment Letter, which was submitted to the SEC in response to the Reg AB II Proposal.[25]

As indicated above, the SEC has yet to issue final rules for stress testing scenarios. If the U.S. requirements for waterfall information are modified to require issuers to provide computer models, unintended consequences may arise with respect to cross-border transactions. For example, non-U.S. issuers might leave the U.S. public market and only operate in private or non-U.S. markets to avoid a potential increase in liability. Additionally, if Regulation AB II is adopted as proposed, it will create another disparity between the disclosure requirements of U.S. and European markets. This differential treatment between the E.U. and U.S. might create transactional costs to European issuers interested in placing their ABS both in the U.S. and in the European markets because they will also have to comply with U.S. standards. In a globalized economy with issuers and investors in a variety of jurisdictions, the existence of two different regulatory regimes for stress testing the same product will create inefficiencies and transactional costs triggered by dual compliance. Moreover, foreign issuers will lose incentives to participate in the U.S. market because they will be subject to a higher standard of liability in connection with stress testing information. This could negatively affect the liquidity of ABS in U.S. markets and could harm both issuers and investors.

Alternatively, if Regulation AB II is not adopted in the U.S., the European markets may suffer a similar negative effect because, even though they have lesser stress testing requirements than those proposed in Regulation AB II, there will still be transactional costs associated with the disclosure requirements of Article 122a. Non-E.U. issuers wishing to sell to European Regulated Investors will have to comply with dual regulations regardless of whether or not Regulation AB II is adopted as proposed in the U.S.

C. Conclusions on stress testing information

Because the Reg AB II Proposal has not yet been adopted by the SEC, it is somewhat premature to discuss the frictions between U.S. and E.U. stress testing regulations. Therefore, we encourage IOSCO to wait until the U.S. regulators have, at least, stated their final position in connection with the Reg AB II Proposal before taking a position on this matter. It is possible, for example, that the SEC chooses to follow the more market-driven approach to stress-testing called for by Article 122a as currently in force in the E.U., resulting in a relatively consistent framework across jurisdictions.

Since the term "stress testing" has not been technically defined and is subject to varying interpretations depending on, among other things, market needs, we recommend that IOSCO recommend including in any global standards a definition of this term based on broad considerations. A variety of analytic approaches can be applied to the interpretation of this

[25] *See* http://www.americansecuritization.com/uploadedFiles/ASF_Reg_AB_II_Waterfall_Comment_Letter_8.31.10.pdf.

concept and, thus, including a detailed legal definition that adopts only one approach might result in an interpretation that is not adaptive to market and investor needs. In any event, any recommendation on stress-testing for ABS should be based on input from a wide spectrum of market participants, including not only inventors (who may not be as sensitive to the indirect impacts of inappropriate stress testing on an originator's securitization activity) but also originators and others, so that a thorough cost-benefit analysis of any recommendation can be developed.

Further, even if relatively different approaches were taken in the U.S. and the E.U. in connection with stress testing, the global standards to be promoted by IOSCO do not necessarily have to tend towards harmonizing stress testing information requirements. In particular, we feel that it would not be appropriate in the much more litigious U.S. environment to expect or require originators of ABS sold in the U.S. to have responsibility for selecting the relevant inputs for any stress-testing model used by investors for that originator's ABS. Once the U.S. has finalized its regulatory standards relating to stress testing, IOSCO may wish to promote a Passporting model similar to the approach discussed in the "risk retention" portion of this letter.

IV. <u>Standardization</u>

A. Introduction

The portions of the IOSCO consultation report dedicated to standardization reference two key areas for discussion: the standardization of ABS disclosure documentation generally and the harmonization of loan-level data. While ASF recognizes the importance of harmonizing loan-level data requirements where possible, attempts to achieve the standardization of disclosure generally could have a negative impact on cross-border activity.

A. Disclosure Generally

Regarding disclosure generally, the IOSCO consultation report notes that most jurisdictions do not specify any standardized disclosure formats. ASF strongly encourages IOSCO to recommend that the industry develop "best practice templates" and not to differentiate between the harmonization of disclosure generally and the harmonization of loan-level data across jurisdictions.

However, ASF believes it is important to address the difficulties that could arise from a general standardization requirement. Because of the disparity in the way information is presented across jurisdictions (*i.e.*, the "plain English" requirement of the SEC for U.S. disclosure documents and the formalities of the Prospectus Directive in Europe) as well as the disparity of information disclosed for particular types of ABS, a standardized form document would likely present extraordinary challenges for originators and other securitizers.

Additionally, because information relating to various ABS classes differs with each particular ABS, the potential benefit to investors is uncertain. Even the standardization of definitions across jurisdictions or types of asset classes could create difficulties (as an example, if the term "delinquency" in reference to a loan were given the standard meaning of 30 days past

due, this could interfere with specific industry practices and could prevent securitizers and investors from shaping the individual terms of a transaction to fit specific needs). Ultimately, the idea of a standardized form for ABS that presents information in the exact same way across jurisdictions and ABS classes may be appealing in theory, but it is not likely to improve investor confidence in the market and could easily create several practical implementation problems for securitizers that could obstruct market activity.

B. Harmonization of Loan-Level Data Requirements

ASF supports efforts to harmonize loan-level data requirements between the U.S. and Europe through the standardization of disclosure documents. Harmonization can benefit investors by easing the process of comparison between different investment opportunities across jurisdictions. However, it is important to note that the different characteristics of the U.S. and European markets and the widely different characteristics of individual asset classes means that a prescriptive approach to disclosure requirements without consideration for these differences could have an overall negative impact on the markets. Therefore, we encourage IOSCO and other regulators to broadly endorse a principles-based approach to standardized disclosure requirements. A principles-based approach would allow for a more flexible common standard between jurisdictions and avoid potential complications and negative side effects that a prescriptive list of requirements could cause.

A comparison of current legislative and industry-driven initiatives in Europe and the United States demonstrates the potential challenges to standardizing disclosure requirements across markets.

C. Standardization of Disclosure Requirements in Europe

i. Article 122a

Paragraph 7 of Article 122a requires one of the sponsor, originator, or the original lender to provide investors with readily available access to all materially relevant data on the credit quality and performance of the individual underlying exposures. The CEBS Guidelines clarify that this will typically mean that "loan-level" data will be required, although in securitizations with a large number of highly granular exposures it may be appropriate to disclose data on a collective basis.

The CEBS Guidelines are not prescriptive on an asset class basis. In practice, this means that different asset classes, particularly those where no market standard loan level data template has been developed, are allowed a degree of flexibility when implementing the disclosure requirements of Article 122a.

ii. Other Non-Legislative Initiatives

In recent years, the ECB and the Bank of England have implemented new policies with the objective of increasing the level of, and standardizing, loan-by-loan disclosure for ABS offerings. These new requirements seek to standardize disclosure by providing templates for

originators to use that set forth the information to be provided by originators to investors. Importantly, in their attempt to promote standardization across ABS disclosure requirements, the central banks have recognized that differences exist between classes of ABS. The central banks addressed these differences by providing different template documents for the various classes of ABS. Additionally, because the central banks recognize that disclosure requirements should not unduly limit the availability of ABS to investors, they adopted a "comply or explain" approach when originators cannot provide information required by these new disclosure requirements. As discussed below, these requirements are being implemented for different classes of ABS on a graduated schedule.

a. The European Central Bank

In December of 2010, the ECB announced it would make loan-by-loan disclosure a requirement for ABS in order for these securities to be eligible for the Eurosystem collateral framework. A template for loan-level data disclosure for residential mortgage-backed securities is available on the ECB website.

b. The Bank of England

In 2010, the Bank of England stated it intended to introduce a set of requirements that required loan-by-loan information to be made available to market participants at regular intervals at least quarterly and on standardized templates provided by the Bank of England for each asset class. These disclosure requirements are more comprehensive than those required by the ECB. In addition to loan-by-loan disclosure, the Bank of England also requires a transaction summary setting out all the key features of the transaction, standardized monthly investor reports made freely available, and a waterfall cash flow model.

These provisions were first implemented with regard to RMBS in November 2011 with a twelve month transitional period. Even with the new requirements being limited to one class of product and given a one year implementation period, standardization was still extremely difficult.

c. "Comply or Explain" Approach

After trade associations in the European markets raised concerns regarding these new requirements, both the Bank of England[26] and the ECB[27] adopted a "comply or explain" approach to their respective disclosure requirements. This approach addresses one of the main concerns voiced by European trade associations: that a blanket application of disclosure requirements could preclude the availability of certain asset classes for investors when originators are not able to provide the requested mandatory information. Overall, the "comply or explain" approach

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[26] Bank of England, *Market Notice – Detailed Eligibility Requirements for Residential Mortgage Backed Securities and Covered Bonds Backed by Residential Mortgages*, July 19, 2010, *available at* http://www.bankofengland.co.uk/markets/Documents/marketnotice101130abs.pdf.

[27] European Central Bank, *Transmission of ABS Loan-Level Data*, last accessed July 10, 2012, http://www.ecb.int/paym/coll/loanlevel/transmission/html/index.en.html (see RMBS tab).

adopted by the Bank of England and ECB seems to allow for increased loan-by-loan disclosure requirements, but through a flexible, principles-based approach, which ASF supports.

D. Standardization of Disclosure Requirements in the United States

i. Legislative Initiatives

Following the financial crisis, the U.S. passed Dodd-Frank, which prompted the SEC to implement a range of new disclosure requirements intended to provide investors with greater consistency of disclosure across ABS products and markets.[28] Further, in the Reg AB II Proposal, the SEC proposal to standardize disclosure across ABS markets by effectively requiring compliance with all of the technical requirements of Regulation AB in most privately placed transactions. This element of the Reg AB II Proposal was met with particularly strong criticism by market participants. The SEC has not formally adopted Regulation AB II and the state of disclosure requirements in the U.S. remains uncertain. While it is unclear exactly what originators of ABS may have to disclose in the future, it is clear that the SEC supports measures that promote disclosure in a more harmonized (if not "standardized") way. Although this approach would make disclosure more consistent across markets in certain areas, in order for disclosure measures to result in an increase in investor activity, market participants in the U.S. also recognize that it is important that standardization or harmonization efforts do not preclude certain ABS from the market due to an inability to comply with rigid and technical disclosure obligations.

ii. Non-Legislative Initiatives

a. ASF's Project RESTART

ASF launched the *Project on Residential Securitization Transparency and Reporting* ("*Project RESTART*" or "*RESTART*") on July 16, 2008 in order to help rebuild confidence in mortgage- and asset-backed securities and to restore capital flows to the securitization markets.[29] Since its launch, *RESTART* has been recognized by senior policymakers and market participants as a necessary industry initiative to improve the securitization process by developing commonly accepted and detailed standards for transparency, disclosure and diligence. ASF members participating actively in *RESTART* include institutional investors, issuers, originators, financial intermediaries, servicers, rating agencies, due diligence professionals, trustees, outside counsel, outside consultants, and data modelers and vendors.

On July 15, 2009, ASF released final versions of the first two deliverables of *RESTART*, a disclosure package of loan-level information to be provided by issuers prior to the sale of private-label residential mortgage-backed securities ("RMBS") transactions (the "ASF RMBS Disclosure Package") and a reporting package of loan-level information to be updated on a

[28] An example is Rule 15Ga-1, which requires securitizers to disclose demands for asset repurchases due to breaches (or alleged breaches) of representations and warranties in the transaction documents and which applies to both public and privately-placed transactions.

[29] *See* www.americansecuritization.com/restart.

monthly basis by RMBS servicers throughout the life of an RMBS transaction (the "ASF RMBS Reporting Package"). Next, on December 15, 2009, ASF released the "ASF Model RMBS Representations and Warranties,"[30] which establish a set of standardized representations and warranties to serve a baseline model in the production or assessment of the representations and warranties set forth in securitization governing contracts going forward. On August 30, 2011, ASF released the latest deliverable, the "ASF Model RMBS Repurchase Principles,"[31] which set forth a third-party mechanism to ensure that representations and warranties in future RMBS transactions are subject to clearly defined enforcement mechanisms.

E. Challenges of Standardization across Jurisdictions

While both the United States and Europe are attempting to promote greater standardization of disclosure requirements for ABS transactions, the differences in legislative and non-legislative initiatives between the two jurisdictions demonstrates the differences in need for the two markets. Much of the focus of standardization in the U.S. has been focused on the residential mortgage market, which was a key source of problems during the 2008-2009 financial crisis in the U.S., whereas European standardization efforts have been broader based, and focused on more general themes of consistency of approach across markets.

In addition to differences between the markets, there is generally a degree of non-comparability between different types of securitizations that makes standardization challenging. For example, it would be difficult, if not impossible, to provide something like a consistent "Need to Know Sheet" used by investment funds for ABS transactions involving residential mortgages, auto loans, credit cards, and commercial loans due to the significantly different structures used to securitize these assets.

Unduly standardizing disclosure requirements can drive actual lending behavior (for example, if all securitized loans had to have particular terms, this could restrict what loans are available to consumers by discouraging certain types of loan instruments). Even the standardization of definitions could force some products out of the market or limit their availability to investors, which would have a dampening effect without a clear benefit.

The development of consistent definitions and terminology also pose an issue for standardization because of the challenges in changing established definitions in their respective jurisdictions at this stage. It might not be possible to achieve standard definitions and it is unclear how these could be implemented without accompanying regulatory authority.

While there are several legislative and industry-developed initiatives currently aimed at promoting the standardization of disclosure for ABS transactions, the implementation of prescriptive requirements poses challenges across markets. Because many securitized assets classes utilize different structures and formats (such as master trusts, ABCP structures, varying forms of credit support and the like) and because the needs of different jurisdictions vary with

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[30] *See* http://www.americansecuritization.com/uploadedFiles/ASF_Project_RESTART_Reps_and_Warranties_121509.pdf.

[31] *See* http://www.americansecuritization.com/uploadedFiles/ASF_Model_RMBS_Repurchase_Principles.pdf.

the demands of different markets, IOSCO should encourage harmonization by adopting a more principles-based approach to standardization.

V. Conclusion

ASF has been a strong and vocal advocate for targeted securitization market reforms and we continue to work with regulators to identify and implement them. We stress the significant impact of the securitization market on the real economy as outlined above. Therefore, we strongly support efforts to align international regulatory approaches to risk retention, transparency and disclosure standardization in order to minimize hampering inefficiencies and costly frictions in cross-border securitization transactions caused by diverging regulatory regimes that could negatively affect the real economy's access to securitization-related financing.

ASF will continue to work to provide industry comment on all proposals issued by the various regulatory agencies as well as to promulgate best practices for securitization governance in order to restore confidence in this very important market. Where regulators are tasked with implementing reforms, we support uniform implementation across jurisdictions, where appropriate, supported by comprehensive industry and public comment.

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ASF very much appreciates the opportunity to provide the foregoing comments in response to IOSCO's Consultation Report. 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, Evan Siegert, ASF Managing Director, Senior Counsel, at 212.412.7109 or at esiegert@americansecuritization.com, or Lewis Cohen, Clifford Chance LLP, at 212.878.3144 or at lewis.cohen@cliffordchance.com.

Sincerely,

Tom Deutsch
Executive Director
American Securitization Forum