



August 2, 2010

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

RE: Asset-Backed Securities (Release Nos. 33-9117; 34-61858; File No. S7-08-10)

Ladies and Gentlemen:

CoStar Group ("CoStar") appreciates the opportunity to comment on the Securities and Exchange Commission's ("SEC" or "Commission") proposed revisions to Regulation AB (the "Proposed Rule"). We support the Proposed Rule and believe that much of the recent economic crisis could have been avoided if better processes had been in place prior to and at the time of our financial market meltdown. Accordingly, we applaud the Commission for its effort to reshape the landscape of financial practices and regulation.

While we support the steps that the Commission is taking to implement better practices, including requiring new issuance offering content, we respectfully recommend that the Commission consider adopting the following modifications prior to adopting the regulation as final:

- **Performance Data.** We recommend that the Commission require additional data fields for Commercial Mortgage-Backed Securities.
- **Cash Flow and Waterfall.** We support the creation of a waterfall program and provide recommendations for enhancing the program's design and interface.
- **Timely Dissemination.** We recommend that the Commission require disclosure at the time of "observable events."
- **SEC EDGAR Database.** We recommend that the Commission not serve as the repository for data, and that it establish another clearinghouse.

I. Background

CoStar provides commercial real estate information services to all members of the commercial real estate industry, including investors, owners, and lenders. CoStar is an independent third-party service provider with respect to commercial mortgage-backed securities. We are neither an issuer nor an

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investor; however, both issuers and investors utilize our products and services in relation to either offering commercial mortgage-backed securities or investing in them.

II. Recommendations

A. Require More Data Fields for CMBS:

Commercial Mortgage-Backed Securities ("CMBS") market participants consider their practices to be "best-in-class," with arguably the best disclosures and processes among the asset-backed security asset classes. In light of this, and given our familiarity with the data currently made available to the CMBS investment community, we believe that the Proposed Rule reflects a step in the right direction, but falls short of the stated goal of providing sufficient transparency to investors. As such, we urge the SEC to include all data fields specified in the CREF Council CMBS Requirements. This is not burdensome for issuers to provide – they already collect this data.¹

Firms engaged in originating, billing and collecting the underlying collateral have already identified and put their financial resources behind maintaining the data fields² they think are important for valuing, monitoring and collecting the collateral. Given the depth of knowledge and experience of these industry participants, we urge the SEC to carefully weigh existing practices and formulate a final rule that reflects those practices. We are concerned that, if adopted as proposed, the final rule will require disclosure of a mere subset of the information that is otherwise gathered and available. And, we believe that adding this data would impose a minimal cost on issuers to comply.

B. Enhancements for the Cash-Flow Waterfall Program Requirement

We support the SEC's creation of a waterfall program in the Proposed Rule and believe that it is consistent with the twin goals of providing enhanced transparency and leveling the playing field for all investors.

Current industry practice forces investors to rely on third-party providers to model cash-flow waterfall priorities. This practice, of which CoStar is an indirect beneficiary, has ramifications for both investors and third-party providers. We point these out below in comparing a publicly available waterfall program with the use of third-party providers:

1. **Cost.** Reliance on third-party providers creates an unnecessarily uneven playing field among investors. These services are generally costly, and the fee structures are not sufficiently

¹ We have included a very short list, by way of example of missing fields in Attachment 1. They are intended as examples of critical information obtained by issuers that are not contemplated to be required under the Proposed Rule. It is clear that the example missing fields are critical for investors to assess the risk of a CMBS bond. We reiterate that it is unnecessary to make a decision regarding which data should be disclosed; the issuers already collect the data and all of the data should be made readily available to the entire marketplace.

² Standard CMBS requirements as established by Commercial Real Estate Finance ("CREF") Council.

flexible to meet the needs of investors and analysts with different appetites with regard to volume, credit exposure, or purpose.

2. **Reliability.** Our experience in securitization analytics indicates that the mechanics of directing the cash-flow according to the legal documentation can be improved. We recommend that the SEC require issuers that create the securitizations provide all investors with an accurate program to apply estimated collateral performance through the securitization structure; and impose commensurate liability for inaccurate program results. If issuers are not able to produce such a program, we question whether the securitization meets the reliability test.
3. **Efficiency.** Many third-party services developed their architecture more than a decade ago, and as securitizations structures and credit risk analytics have evolved, these systems have struggled to keep pace. When creating models to reflect the new challenges facing the collateral, we sometimes encounter significant obstacles when interfacing with these dated systems. Reliance on this arguably stale architecture prevents timely analysis of securitized bonds, and imposes an unnecessary risk on the marketplace. By allowing participants to plug into a new, industry standard interface for prioritization of cash-flows, industry participants will act at a faster pace to improve the analytics necessary to develop a more efficient market.
4. **Competitiveness.** We believe that concerns regarding harm to existing third-party servicers from the waterfall program are arguably misplaced. We reach this conclusion for two reasons. First, providing the cash-flow waterfall program to all investors and analysts would open the playing field to a broader array of investors and would compel existing providers to improve their systems to remain competitive. Second, many current investors have third-party providers' systems embedded into or otherwise integrated into their analytic systems. It is unlikely that a material portion of these investors would suddenly replace the existing developed interfaces. As a third-party provider ourselves, we caution against protecting the *status quo* at the expense of moving toward better capital formation, which should be the ultimate goal of Proposed Rule.
5. **Programming Language.** Although many raise concerns about the choice of "Python," we support the SEC's "open source code" requirement, and make the following suggestions for enhancing the program:
 - a. **Consistent Model Design:** A standardized design format (model design specs) would result in consistent model design ("look and feel") from one deal to another that would allow investors to quickly download and analyze any deal without having to get refamiliar with a new model design and figure out how the inputs and outputs work, where the buttons to drive the model are, etc.
 - b. **Consistent/Useful Interface (Input/Output):** The model should, at a minimum, allow for standardized inputs (aggregated deal level cash-flow on either a daily or

monthly basis, as well as non-cash adjustments to waterfall priorities, such as appraisal reductions) and outputs (the resultant application of the collateral cash-flow and non-cash waterfall adjustments through the bond structure, including identification of interest and principal shortfalls, including their cumulative balances, over time) in excel format³. The model should also anticipate potential cash-flow streams that exceed the final underlying collateral maturity date by at least ten years; the extension and modification of underlying collateral loans is likely to play out for several years beyond the original anticipated maturity dates. Since flexibility regarding inputs and outputs are critical for successful analytics, this aspect of the design should be approved by key constituencies including a representative investor group.

- c. **Clearly Articulated Waterfall Rules Including Diagrams and Flowcharts:** Investors should not buy what they cannot understand. This point cannot be overstated. If investors follow this dictum, they would limit their investments to those transactions where they can understand the structural features of the transaction. Under current practices, information is generally limited to the legalese in sales agreements regarding the prioritization of cash flow. This is inadequate and unnecessarily inefficient. In addition to providing an open source code program for analyzing potential outcomes based upon collateral performance, investors should be provided with visual descriptions of the priorities of the cash flow waterfall in the form of diagrams and flowcharts.

C. Require Updates at “Observable Events”

If investors had been made aware of the rapidly souring performance of sub-prime mortgages in a timely manner, they would have rejected new issuance at the peak of the market, thereby avoiding much of the damage from the economic crisis. Notwithstanding this, trustees and servicers of the underlying collateral continue to limit the dissemination of this data. In an effort to protect themselves, some investors contract trustees and servicers directly for information, gaining what is arguably an unfair advantage over other unsuspecting investors that are unaware of this practice.

To address these concerns, we urge the SEC to establish clear rules that, with respect to a loan or receivable that is an underlying exposure for a securitization transaction, any "observable event" relating to such loan or receivable should be disclosed on the day the "observable event" occurs or as promptly thereafter as possible. An "observable event" means, with respect to a loan or a receivable that is collateral for a securitization, any of the following: 1) payment (and the amount thereof) by the obligor on such loan or receivable; 2) failure by the obligor to make payment in full on such loan or receivable on the due date for such payment; 3) amendment or other modification with respect to such

³ Excel is as close to a financial industry standard that crosses the spectrum from participants possessing very sophisticated analytic tools to those possessing less sophisticated analytic tools.

loan or receivable; 4) the billing and collecting party becomes aware that such obligor has become subject to a bankruptcy or insolvency proceeding; or 5) the reporting of any other action that may influence the collectability of the collateral or the resultant cash waterfall through the bond structure (examples: a foreclosure action by the servicer, an appraisal reduction, the sale of collateral by the servicer, or the extension of funds for the protection of an asset).

Reporting based on the occurrence of an observable event (rather than the current practice of end-of-month reporting) has three fundamental advantages:

1. It is consistent with how observable events are tracked and reported by the databases that track the daily billing and collecting of the underlying loans and receivables. This same expertise and frequently the same information systems can be used to support observable event-based reporting for securitizations.
2. Observable event-based reporting allows investors to monitor performance of the loans and receivables supporting a securitization as frequently as they would like and, when they do, to know what they own currently. Investors will have the choice of how frequently they want to monitor performance. Denying investors the ability to monitor observable events as they occur is counter-productive as it does not restore confidence and as a result diminishes the interest in and investment appetite for securitizations.
3. Observable event-based reporting eliminates the informational asymmetry and the related informational advantage of the firms participating in originating, billing and collecting these or similar type loans and receivables of the type that are collateral for securitization transactions.

D. Use a Clearinghouse for the Repository

We believe that serious concerns exist regarding the SEC acting in the role of the repository of asset-backed security related data. We believe that the SEC may find itself with a conflict of interest if the Commission acts to both regulate the industry and provide a service function for the industry. We believe the better approach is to create a clearinghouse that fulfills the singular purpose of maintaining an accurate, up-to-date repository of data for the industry relative to asset-backed securities.

All firms, including their investors who can influence their activities, directly involved in managing the clearinghouse would be required to make a full disclosure of all competitive and financial interests in the design of the database, the presentation of the data, the analysis of the data and the use of the data including whether the firm engaged in a related business that could gain a competitive advantage from its role and whether the firm has investments that could benefit from its role.

III. Conclusion

The primary goal of the Proposed Rule is to enhance investor protection by providing investors with timely and sufficient information. We agree with this goal, and believe that every effort should be made

to improve transparency for asset-backed securities. This means free-flowing, all-inclusive data delivered on an expedient basis.

Wholesale change is requisite in the aftermath of failure to provide, monitor, and regulate a functionally sound marketplace. Vested interests of various market participants, whether they be the former investment banks, issuers, rating agencies, regulators, or third-party service providers must take a back seat in the best interest of creating a sound, reliable, trustworthy, and efficient market. We embrace such a change – it is critical to the formation of much needed capital for key pillars of our economy.

CoStar Group appreciates the opportunity to comment. We support the proposed rule and believe that the regulations should go further towards the goal of increasing transparency. We are available to discuss these suggestions at your convenience. You can reach: John O'Callahan, Steve Miller or Mark Fitzgerald at 617-426-4446.

Respectfully submitted,

A handwritten signature in cursive script that reads "John O'Callahan". The signature is written in dark ink and is positioned above the printed name and title.

John O'Callahan, CFA
Capital Markets Strategist

ATTACHMENT 1

EXAMPLES OF MISSING FIELDS

- 1. Rent Roll.** Rent rolls contain the information necessary to fully estimate the potential cash flow generated by a property to pay the mortgage payment. Rent rolls are gathered and reviewed at initial underwriting and are the most critical element in evaluating a commercial real estate loan. Accordingly, we recommend that the SEC adopt in the final rule a requirement to disclose: (i) tenant name (unless a residential property); (ii) tenant business line; (iii) lease start date; (iv) lease amount including any concessions or associated expenses such as tenant improvements; (v) expense sharing arrangements; (vi) co-tenancy clauses; and (vii) lease renewal options. We believe this would be the single most important set of data disclosed with respect to a loan collateralized by a commercial property.⁴
- 2. Reserves.** Reserves can be held for payment of interest shortfalls, tenant improvements, leasing commissions, capital improvements, real estate taxes, and more. Application of reserves also typically requires that certain conditions be met, therefore some reasonable description of these requirements are important as well.
- 3. Unfunded Commitments.** The unfunded commitment disclosure should include the amount of the unfunded commitment and any requirements relative to funding, and expiry.
- 4. Related Lien Information.** Default risk is a function of the total amount of liens on a property (or on multiple properties). It is critical that investors have sufficient information on all related liens existing for each loan in the securitization, *i.e.*, 2nd liens, mezzanine debt, *pari passu* loans. This information should be updated regularly so that investors are aware of newly originated additional liens on the same property. In addition, there should be clear disclosure about the capacity and eligibility criteria that would allow the borrower to place additional liens on the property in the future.

⁴ We note that the Proposed Rule requires disclosure of information relating to the largest three tenants, which, in the case of larger properties, may constitute only a fraction of the potential income stream. 75 Fed. Reg. 23,364 (May 3, 2010). We believe that our above recommendations will provide the marketplace with more useful information.