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August 2, 2010

By e-mail: rule-comments@sec.gov

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: Proposed Rule on Asset-Backed Securities
File Number S7-08-10

Dear Ms. Murphy:

We are submitting this letter in response to the request of the Securities and Exchange Commission (the "Commission") for comments regarding the Commission's proposed rules (the "Proposed Rules") on asset-backed securities ("ABS") contained in Securities Act Release No. 33-9117 (April 7, 2010); 75 Fed. Reg. 23328 (May 3, 2010) (the "Proposing Release"). We appreciate the opportunity to provide comments on the Proposed Rules.

We are supportive of the Commission's efforts to enhance the ability of investors to analyze and evaluate ABS and other structured finance securities. However, as described in this letter, we are concerned that certain of the Proposed Rules may have unintended and adverse effects on liquidity in the institutional market, i.e. with respect to transactions presently effected under the registration safe harbors of Rule 144A, Regulation D and, to a lesser extent, Rule 144 under the Securities Act. Our comments focus primarily on the specific provisions of the

Proposed Rules that we see as raising issues for non-registered ABS and structured finance transactions.

1. The Commission should condition the registration safe harbors on the availability of information that would be required in a public offering only to the extent the issuer possesses such information or can obtain it without unreasonable effort or expense.

The Commission proposes to condition the availability of registration safe harbors under Regulation D, Rule 144 and Rule 144A on requirements to provide to investors in ABS or other structured finance transactions, upon their request, "information as would be required if the offering were registered on Form S-1 or Form SF-1 under the Securities Act and any ongoing information regarding the securities that would be required by Section 15(d) of the Exchange Act if the issuer were required to report under that section."[1] The Commission notes in this regard that "many have asserted that the lack of information about CDOs and other structured securities in the private market exacerbated the harm to investors and the markets as a whole during the financial crisis." [2] While it may be desirable to specify a minimum level of information that should be available to investors in Rule 144A transactions, fixing that minimum at the same level as that applicable in a registered offering is likely to unnecessarily limit the flexibility of the private placement option for both safe-harbored and non-safe-harbored transactions, impose unnecessary costs on issuers and investors and impair the ability of investors to effect resales of privately placed securities. We believe the Commission should enact a more flexible standard rather than so closely equating the information mandated to be provided to institutional investors to the requirements of a registered transaction.

Flexibility of Disclosure is a Beneficial Feature of the Private Placement Markets

As the Commission notes, "[a]n assessment of whether the protections of the Act are needed traditionally focuses on whether the purchasers of securities can 'fend for themselves'" and "[h]istorically, whether this test is met turned on whether information necessary or appropriate to make informed decisions is realistically available to the purchasers."[3] Thus, the availability to an investor of disclosures necessary to make an informed investment decision is not an express requirement, but is a premise, of Rule 144A. The basis for Rule 144A is that investors in the institutional market have the ability to demand the information they need.[4]

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[1] Proposing Release, 75 Fed. Reg. at 23436. We focus our discussion here on the new conditions to Rule 144A. The similar conditions to Regulation D and Rule 144 raise similar issues, but less so given the importance of Rule 144A to the institutional market.

[2] Proposing Release, 75 Fed. Reg. at 23394.

[3] Proposing Release, 75 Fed. Reg. at 23333 n.58 (citing SEC v. Ralston Purina Co., 346 U.S. 119, 125 (1953)).

[4] See, e.g. Rel. No. 33-6806 ("Initial Rule 144A Proposing Release"), 53 Fed. Reg. 44016, 44026 (November 1, 1988) ("The key to the analysis of proposed Rule 144A is that certain institutions can fend for themselves and that, therefore, offers and sales to such institutions do not involve a public offering."); Van Dyke v. Coburn Enterprises,

Accordingly, under Rule 144A as currently in effect, only the most basic information concerning the issuer is required to be provided. Similarly, under Regulation D as currently in effect, issuers are not required to furnish any particular information to purchasers that are accredited investors. In neither market has this led issuers to abandon the practice of providing extensive disclosure to prospective investors. This is due primarily to two factors: the desire of issuers and underwriters to avoid liability under Rule 10b-5, and the power of sophisticated purchasers to demand that they receive sufficient information to make an informed investment decision. But while the practice in the private placement markets has been to provide extensive disclosure, the flexibility to vary that disclosure from what would be required in a registered offering is one of the most beneficial features of private placements to both issuers and investors.

One of the most compelling reasons that issuers turn to the private placement markets instead of conducting a registered public offering is that they are unable at a given time to satisfy all of the formal requirements of registration, or are unable to do so without inordinate effort or expense. For example, issuers that are temporarily unable to provide financial statements that comply fully with Regulation S-X (perhaps due to a delayed audit report or pro forma statements) have been able to obtain necessary financing by disclosing to private placement investors the circumstances of that inability and including such financial information as they are able to provide. It is important to remember that even in the absence of requirements such as those in the Proposed Rules, private placements do not proceed unless an issuer and its advisors conclude that whatever information they are able to provide is sufficiently robust as not to contain material omissions, and such private placements do not succeed unless sophisticated investors concur that the information provided is sufficient. In the context of a private placement, investors can also negotiate the terms of the security to compensate for any information that is lacking or inadequate, for example by requiring better economic terms to compensate them for the incremental risk or by demanding additional covenants or reports on an ongoing basis. The ability for issuers and prospective investors to, in effect, agree on the adequate level of disclosure for a given circumstance is a crucial and extremely beneficial feature of the private placement markets. Issuers decide what level of disclosure they can reasonably provide, and investors decide for themselves whether that level of disclosure is enough. Any investor that finds the disclosure insufficient simply doesn’t purchase, and if the market consensus is that sufficient information isn’t available, no transaction is consummated.

The Proposed Rules Would Impose Unnecessary Costs on Issuers

The requirement of the Proposed Rules that investors receive, *upon request*, information the same as that made available in a registered offering under Regulation AB or Form S-1 will in practice have the effect of requiring issuers to prepare such information if they wish to avail themselves of the safe harbor, whether or not any investor finds it relevant or ever requests it. In other words, the “upon request” qualification of the Proposed Rules is an illusory limitation.

Inc., 873 F.2d 1094, 1098 (8th Cir. 1989) (exempt transaction found where “appellants had the economic bargaining power to demand any information necessary to make an informed investment decision”).

At the stage of the initial offering, issuers wishing to qualify for a safe harbor will want to ensure that their placement can proceed smoothly, without incurring delays if additional information is requested; thus, they will prepare the full range of information in advance to obviate the risk of facing a choice between losing the safe harbor and delaying an offering because a single prospective investor has made a request for information that other investors deem unnecessary.

The Proposed Rules will have a similar effect through the life of the transaction. This is because the Commission has specified in the Proposed Rules that any prospective transferee of a Rule 144A "structured finance product" has a right to request "reports that would be required by Section 15(d) of the Exchange Act if the issuer were required to report under that section." In ABS transactions, it is necessary to determine and specify at the outset exactly what asset characteristics will be monitored and reported periodically, in part so that the trustee or servicer charged with assembling that information can establish appropriate systems and ensure that it can comply with the requirements. Accordingly, under the Proposed Rules, prudent issuers will likely require the full range of Regulation AB information to be monitored and reported by the trustee or servicer from the beginning, whether or not it is ever requested, because failure to do so puts the transaction at risk of violating the law if a holder makes a request that cannot be adequately responded to, whether because it is outside the scope of the trustee's or servicer's agreed duties or because collecting the necessary information on a retrospective basis proves impracticable. Even if issuers do not require this, it is likely that the initial investors will, because the only realistic way in which the initial investors will be able to ensure that they can later transfer their securities under Rule 144A is to require issuers to put in place registered-equivalent disclosure and reporting at the time of initial issuance of the relevant securities, whether the investors in the transaction actually want to bear the costs associated with such reporting or not. And it is certainly the investors who will bear this incremental expense, because the fees of the trustee and servicer are paid from distributions on the securitized assets.

The Proposed Rule Would Adversely Affect Private Placements Outside the Safe Harbors

The Commission acknowledges the incremental burden that the Proposed Rules will have on safe-harbor transactions, but appears to consider that issuers and underwriters (in initial placements) and institutional investors (in resale transactions) will be able to rely on private placement transactions outside the safe harbor rather than Rule 144A. As the Commission notes, "structured finance products issuers may conduct offerings in reliance on a statutory exemption under the Securities Act without seeking the safe harbor provided by Rule 506 of Regulation D or without representing that the securities are eligible for sale under Rule 144A" and "our proposed amendments to the safe harbors would not apply to these offerings." [5] However, as the Commission noted when adopting Regulation AB, "[a] new line item disclosure requirement represents [the Commission's] judgment that an item is or has become material."[6] Accordingly, the consequences of the extensive new disclosure and reporting requirements adopted for

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[5] Proposing Release, 75 Fed. Reg. at 23394.

[6] Release No. 33–8518, 70 Fed. Reg. 1506, 1539 (January 7, 2005) ("Regulation AB Adopting Release").

registered transactions must be understood to have created a new standard for materiality of disclosure. And because a subsequent transferee of securities generally does not have the ability to create new reporting and disclosure requirements not initially put in place in a structured finance transaction, the new standard of material information and disclosure is unlikely to be met in the case of a subsequent transfer of privately placed securities.

The practical lack of access to registered-equivalent information may make a subsequent transfer of privately placed securities unavailable outside Rule 144A. So-called “4(1 ½)” resales have traditionally relied at least in part on an assessment that the information available to a transferee of privately placed securities is substantially equivalent to that available to the initial investors. Prior to the adoption of Rule 144A, resales in the institutional market depended not only on the notion that the institutional investors were sophisticated, but also that the investors “all had access to information about the issuer, an important factor in the courts’ analyses of private offerings.”[7] Therefore, as the Commission changes the standard for materiality in structured finance offerings, a subsequent sale of the relevant security may not be practicable under the “4(1 ½)” standard as previously understood. Again, in the case of an initial placement, the failure of an investor to receive registered-equivalent information in relation to an issuer can reasonably be equated with the investor’s determination not to demand such information. As discussed above, however, after the initial investment, the investor’s ability to request further information from the issuer of an ABS is limited by the bargain initially struck among the transaction participants. A subsequent purchaser can only demand from its upstream seller all the information that seller has a right to obtain regarding the security and its issuer. The purchaser has no direct or greater right to renegotiate the ongoing reporting arrangements with the issuer itself. In crafting Rule 144A, the Commission acknowledged that reality and recognized that encouraging transferability in the institutional market depended on striking a balance: complementing the ability of institutional investors to “fend for themselves” by ensuring that basic financial information must be available to a secondary purchaser before a qualifying Rule 144A resale can be made.

Thus, it cannot be assumed that “4(1 ½)” transfers could take the place of Rule144A in the institutional market. Instead, institutional investors may be forced to provide, in advance, for a costly set of reporting practices that no initial investor in the transaction has actually requested, but which are mandatory for Rule 144A transferability—just as in the case of transactions designed to qualify for the safe harbor as described above. Not doing so may render them unable to effect a resale on a “4(1 ½)” or similar basis due to the traditional standards for such resales.

The Proposed Rule Should Be Modified to Be More Flexible and to Clarify the Consequences of Alleged Non-Compliance

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[7] Initial Rule 144A Proposing Release, 53 Fed. Reg. at 44024 n.120 (discussing *The Value Line Fund, Inc. v. Marcus*). See also ABA Committee on Developments in Business Financing, Resale by Institutional Investors of Debt Securities Acquired in Private Placements, 34 *Business Lawyer* 1927, 1974 (1979) (discussing *Investors Mortgage Group* resale no-action letter in which “the staff required that ‘prospective purchasers . . be limited to persons who have access to the same information about [the issuer’s] stock that a registration statement would provide.”).

For the reasons discussed above, we suggest that the Commission should revise its approach to the extension of registered-equivalent standards to Rule 144A securities. It should first be appreciated just how extensive a change is being made in disclosure and reporting practices, particularly with respect to loan-level data. Just five years ago, the Commission noted in adopting Regulation AB that “a securitized asset pool typically represents obligations of a large enough number of separate obligors such that information on any individual obligor may not be material,” and noted that the requirement for “additional disclosures regarding a particular obligor or group of related obligors when concentration reaches 10%, with more particular disclosures at 20%” was a codification of “longstanding practices.”[8] Admittedly, as the Commission noted in the case of static pool data in 2005, “the growth of technology and the attendant ability to analyze more information means that information that may have not been considered material in the past may now have become material.”[9] Nevertheless, there is a variety of methods that institutional investors may use to obtain and analyze the information considered by them to be material, and no need to mandate the practices for registered transactions as the single standard in the market. For example, many of the requirements of Regulation AB as it exists and is proposed to be amended—such as the exact type and manner in which static pool information is presented, the specific data points used for different assets, the format for waterfall programs, and so on—relate not so much to the substance of the information available to investors as to its format and presentation. Particularly with respect to the specifics of the data points for individual assets, investors may simply wish to take a diversity of approaches.

The Commission should also consider the vagueness and uncertainty that is inherent in the Proposed Rules’ direction that structured finance issuers provide “information as would be required if the offering were registered on Form S-1.” The category of “structured finance products” defined by the Commission that are not “asset-backed securities” includes mostly securities as to which there are few precedents for S-1 registration; indeed in many cases there are none whatsoever. It provides little guidance to state that “the issuer would be required to provide information required under Regulation AB regarding the assets and parties as well as additional information required under Regulation S–K.”[10] On the one hand, basic concepts under Regulation AB such as static pool data, who the appropriate “originator” of an asset or “servicer” of the transaction is, how to disclose asset specific data or performance data, and so on, were simply not intended for structured finance transactions that have detailed management and reinvestment features, or that include assets or exposures in the form of credit derivatives. Nor do the specifications of Form S-1 or Regulation S-K readily lend themselves to structured finance transactions. As the Commission noted in adopting Regulation AB, “the Commission’s corporate offering and disclosure rules were not designed to accommodate some of the special

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[8] Regulation AB Adopting Release, 70 Fed. Reg. at 1547.

[9] Id. at 1539.

[10] Proposing Release, 75 Fed. Reg. at 23396.

characteristics of ABS offerings,"[11] and this statement is no less true of the broader category of "structured finance products" defined in the Proposed Rules than of ABS specifically. As the Commission noted in 2005, Regulation AB was adopted after a long development of "no-action letters, staff comment, market practice and informal staff interpretations," which resulted in an "informal regulatory regime for asset-backed offerings" that was "sub-optimal for a well developed market that represents a large portion of the U.S. capital markets" and "diminished the transparency of applicable requirements, potentially decreasing efficiency and leading to uncertainty and common problems."[12] If structured finance issuers are consigned to consult and apply directly the requirements of Form S-1 and Regulation S-K, even in the Rule 144A market, similar results await at best.

Moreover, while the Commission has now placed importance on information requirements that are independent of asset concentrations, in the institutional market there should be scope for investors to differ in their approaches. The absence of asset-level information at certain concentrations does not necessarily impair an investor's ability to "compare and analyze the underlying asset-level data of a particular asset pool as well as compare them with other pools."[13] For example, an investor may determine that that the cost of reducing smaller components of a loan portfolio to standardized data points is unjustified and that a modeled or worst case assumption may be made as to some individual asset characteristics. There is no reason to assume that such an approach would produce less usable or reliable information.

Finally, while domestic sponsors of public ABS might find it workable, though costly, to conform their practices in Rule 144A issuance to the requirements of registered transactions, compliance with registered-equivalent disclosure and reporting practices can be expected to be a substantial barrier to the participation of foreign sponsors of structured finance products in the Rule 144A institutional market. The Commission should avoid such an unfortunate result. It should be remembered that a principal goal of Rule 144A was to encourage "[f]oreign issuers who previously may have foregone raising capital in the United States due to the compliance costs and liability exposure associated with registered public offerings, and the costs of financing inherent in placing restricted securities."[14]

The Commission should recognize these concerns and revise the new conditions placed on Rule 144A in regard to ABS and other structured finance products. If the Commission feels it necessary to prescribe disclosure standards for the private placement market beyond what the consensus of market participants themselves find sufficient, we urge that the standard acknowledge that some of the detailed, asset-level disclosure mandated by the Proposed Rules will simply not be possible for some issuers, in some asset classes, to compile without expending

[11] Regulation AB Adopting Release, 70 Fed. Reg. at 1584

[12] Id.

[13] Proposing Release, 75 Fed. Reg. at 23355.

[14] Initial Rule 144A Proposing Release, 53 Fed. Reg. at 44022.

levels of time and expense that are simply not warranted by any incremental light the additional information sheds on the investment as a whole.

Before the Commission adopted Regulation D, Rule 146 under the Securities Act provided that investors that did not have special access to issuer information were required to be provided the "same kind of information that is specified in Schedule A of the [Securities] Act, to the extent that the issuer possesses such information or can acquire it without unreasonable effort or expense." The same formulation is used today in a number of rules concerning information required to be furnished in registered offerings. We suggest that a similar approach be taken in this instance. The new conditions should require issuers to provide (in connection with the initial placement) the information that would be required if the offering were registered on Form S-1 or Form SF-1 under the Securities Act, and to provide (on an ongoing basis) the information that would be required by Section 15(d) of the Exchange Act, in each case if requested, *only to the extent that the issuer possesses such information or can acquire it without unreasonable effort or expense*. The virtue of this standard is that it balances the need for information against the difficulty, in time or cost, of providing it. The reasonableness benchmark in this formulation provides a safeguard that accommodates different transaction types and asset classes much better than rigidly prescribed line-item disclosure. If the requested information is routinely prepared by similarly situated issuers in similar transactions, as one would expect if it is fundamental to understanding the investment, then it will be demonstrably unreasonable for an issuer to refuse to provide it. On the other hand, if a particular item of information in Regulation AB would have lesser utility to investors in a particular type of security and consequently is not generally monitored and disclosed or reported, the usefulness of the data to investors would be weighed against the effort and expense involved in collecting it.

We also suggest that the requirements to provide registered-equivalent information should be subject to the qualification that such required information in each case may differ as to format, presentation, or specific loan level data points from the requirements of Regulation AB, and that loan level information may be omitted for one or more portfolio components not exceeding a specified percentage of the relevant portfolio individually and a specified percentage of the relevant portfolio in the aggregate.

In adopting any such minimum information requirement, the Commission should also provide certainty to market participants regarding the consequences of violations of the standard that can be expected to result from uncertainties of translating Regulation AB's detailed loan-level disclosure requirements to classes of assets with very different characteristics. The Commission should provide that a purchase of securities will conclusively establish that the investor has received all of the information it requested—i.e., the condition of the safe harbor has been satisfied. With respect to transfers in the secondary market, the Commission should provide that if an existing investor alleges the issuer has breached its covenant to provide the required information to facilitate a transfer, the investor may seek damages for that breach but neither the investor nor the Commission should be able to claim that this implies the initial placement was not entitled to an exemption from Securities Act registration.[15] An action for

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[15] As discussed below, the Commission has already noted that "a potential claim arising under Section 5 of the Securities Act may not be the appropriate remedy under these circumstances" for failure to satisfy the conditions of

fraud may also be appropriate if it can be shown that the issuer never intended to provide subsequent information on request despite its availability.

We further suggest that as to ongoing information, the requirement to provide Exchange Act-equivalent information should be subject to being waived by a specified requisite vote of the holders of the securities of the issuer as to one or more items of such information, and after the date of any such waiver, information should be required to be provided to a holder or prospective purchaser only for any items of ongoing information for which such requirement has not been waived. The foregoing amendments would preserve Rule 144A's original goal of recognizing the ability of institutional investors to negotiate for themselves the balance between the costs of obtaining information and the need for an adequate basis for their investment decisions, while preserving a substantial and protective minimum standard for the quality of information available in the market as a whole.

2. <u>The Commission should revise the definition of "structured finance product".</u>

While it is hard to gainsay the goal of the Proposed Rules to promote greater investor protection, as already noted there can be costs associated with achieving that goal that ultimately outweigh the benefit of incremental protection. The Proposed Rules' treatment of "structured finance products"clearly raises that concern. First, "structured finance product" is simply not a term used in common industry parlance. Therefore, it is unclear what would be comprised within that term for purposes of the Proposed Rules. Many securities that do not appear to be the target of the Commission's proposal could fall under the umbrella of "structured finance products" broadly construed. These fall into two principal categories. First, there are securities that represent direct corporate obligations of an operating company or parent holding company, and have typically been registered on Form S-3 without reliance on any ABS provisions. Examples include corporate "structured notes," which have principal or interest payments that are linked to one or more interest rate, currency, equity or commodity indices. Many such securities have been issued on a routine basis on S-3 shelf registration statements of the relevant issuer or guarantor. While such securities are generally issued directly by operating company or parent holding company issuers, they may also be issued by special purpose entities guaranteed by such a company. Second, there are securities that may incorporate structured finance-like features such as special purpose entities and fixed income collateral, but ultimately represent corporate debt or preferred stock obligations. Examples include issuers of trust preferred securities, finance subsidiaries holding parent or affiliate debt obligations, covered bond structures, certain types of REITs and others. Congress has already acknowledged this concern in part in the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), providing that the definition of "structured finance product" used there "does not include a security issued by a finance subsidiary held by the parent company or a company controlled by the parent company, if none of the securities issued by the finance subsidiary are held by an

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the safe harbor. Proposing Release, 75 Fed. Reg. at 23436. In this same vein, the clarification we suggest would confirm that compliance with the conditions of the safe harbor should be presumed where an investor proceeds with its purchase.

entity that is not controlled by the parent company.''[16] Nevertheless, the current reach of the "structured finance product" definition may well include such structures. They may be regarded as "collateralized by . . . self liquidating financial assets" and "commonly known" as a "structured finance product."

The dividing line between "structured finance products" and non-structured finance product corporate securities is particularly important given the Commission's currently proposed approach to Rule 144A. Consider for example a repackaging transaction in relation to a corporate bond – i.e. the purchase by a special purpose entity of a corporate bond and the issuance by such entity of securities representing an interest in that corporate bond. Under current Regulation AB such a transaction is treated as an asset-backed security. Where the concentration of credit risk as to a single obligor exceeds 20% in such a repackaging, as in any other ABS, Regulation S-X compliant financial statements must be available, directly or by reference to public reporting, under Item 1112(b) of Regulation AB. Under the Proposed Rules' conditions to Rule 144A for "structured finance products," issuance or transfer of such security would therefore similarly require the availability, upon request, of Regulation S-X financial statements for the issuer of the relevant corporate bond. Outside the context of "structured finance products" however – for example, in a simple Rule 144A transfer of the same underlying corporate bond itself – only the limited financial statement information specified in Rule 144A(d)(4) is required to be available with respect to the issuer. Similar divergent consequences would follow with respect to derivative counterparties or credit enhancement providers relating to a Rule 144A transaction. It therefore makes a great deal of difference for Rule 144A whether a corporate security that has certain "structured finance" features is treated as a "structured finance product."

It does not appear to be the Commission's intent to create a new standard for Rule 144A transfers in relation to securities that are essentially direct corporate obligations, even if they may incorporate structural features or derivative terms similar to those used in certain structured finance transactions. An exception in this regard are credit-linked notes and similar securities, which would appear intended to be included as "structured finance products" even if directly issued by a corporate obligor. We include for the Commission's consideration below a possible alternative set of definitions that is based on the language of the Proposed Rules but would articulate further certain of these distinctions. However, if the Commission does not find our alternative definitions useful, we urge it to clarify in some other manner whether and under what circumstances the Proposed Rules are intended to apply to full-recourse obligations (including those collateralized by financial assets).

"Structured Finance Product" means either a Direct Structured Finance Product or a Synthetic Structured Finance Product.

"Direct Structured Finance Product" means a fixed-income or other security collateralized by any pool of Fixed Income Assets that entitles the security holders to receive payments that depend on the cash flow from such Fixed Income Assets, including without limitation

[16] Section 941 of the Dodd-Frank Act.

(A) an asset-backed security as used in Item 1101(c) of Regulation AB (§229.1101(c)),

(B) a collateralized mortgage obligation,

(C) a collateralized debt obligation,

(D) a collateralized bond obligation,

(E) a collateralized debt obligation of asset-backed securities,

(F) a collateralized debt obligation of collateralized debt obligations;

or

(G) a security that at the time of the offering is commonly known as an asset-backed security.

Notwithstanding the foregoing, a security collateralized or secured by Fixed Income Assets is not a Direct Structured Finance Product if (i) the holder of such security is entitled under the terms of the security (directly or by means of a full and unconditional guarantee, or an undivided beneficial interest in such a direct claim or guarantee) to full recourse for all scheduled payments of principal, interest and other required payments in respect of such security to an Eligible Direct Obligor, (ii) such security is expected to be serviced primarily by payments by such Eligible Direct Obligor rather than payments from the Fixed Income Assets and (iii) such security is not a Synthetic Structured Finance Product.

“Eligible Direct Obligor” means for any security an issuer or guarantor of such security that on the date of issuance of such security would be eligible to make an offering of (1) its non-convertible securities under Form S-3 under the Securities Act or (2) securities exempt from registration under Section 3(a)(2) of the Securities Act.

“Fixed Income Assets” means self-liquidating financial assets such as loans, leases, mortgages, secured or unsecured receivables, or similar debt or fixed payment obligations.

“Synthetic Structured Finance Product” means a Synthetic Security that represents an interest in or is linked to either (A) a Swap for which the underlying reference obligation, deliverable obligations or similar underlying obligations or exposures (whether such obligations may be physically deliverable under such contract or form the basis for valuation or cash settlement) would, if pooled or securitized directly, constitute a Direct Structured Finance Product or (B) one or more Swaps that are linked directly or indirectly to a Swap described in (A), including without limitation any instrument commonly known as a credit-linked note, synthetic credit-linked note, synthetic asset-backed security, synthetic CBO, synthetic CLO or synthetic CDO. Notwithstanding the foregoing, “Synthetic Structured Finance Product” does not include a Synthetic Security that is issued or fully and unconditionally guaranteed by an Eligible Direct Obligor for which the relevant Swap(s) are limited to one or more Swaps commonly known as an interest rate swap, a rate floor, a rate cap, a rate collar, a cross-currency rate swap, a basis swap, a currency swap, a foreign exchange swap, an equity index swap, an equity swap, a weather swap, an energy swap, a metal swap, an agricultural swap, an emissions swap, a commodity swap, or other Swaps not linked directly or indirectly to underlying Fixed Income Assets.[17]

"Synthetic Security" means a security that represents an interest in or is linked, with respect to one or more payments of principal or interest in relation to such security, to a Swap (including without limitation by embedding the features of a Swap in the payment terms of the security).

"Swap" has the meaning set forth in Section 1a(47) of the Commodity Exchange Act.[18]

3. The Commission should consider the FDIC's risk retention provision.

Under the Dodd-Frank Act, the requirement for risk retention or "skin in the game" in relation to securitizations will move beyond the context originally contemplated by the Proposed Rules. The new law requires that "the Federal banking agencies and the Commission shall jointly prescribe regulations to require any securitizer to retain an economic interest in a portion of the credit risk for any asset that the securitizer, through the issuance of an asset-backed security, transfers, sells, or conveys to a third party."[19] The FDIC has already proposed rules to require, as a condition to its securitization "safe harbor" in relation to depository institution issuers, that "the sponsor must retain an economic interest in a material portion, defined as not less than five (5) percent, of the credit risk of the financial assets." Federal Deposit Insurance Corporation, Amendments to 12 C.F.R. § 360.6 Treatment by the Federal Deposit Insurance Corporation as Conservator or Receiver of Financial Assets Transferred by an Insured Depository Institution in Connection With a Securitization or Participation After September 30, 2010, 75 Fed. Reg. 27471, 27485 (May 17, 2010) ("FDIC Proposing Release"). In contrast to the initial FDIC proposal, however, the proposed rule does not necessarily require a retention of risk with respect to the securitization tranches themselves, and gives the option that the originator's retained risk "may be either in the form of an interest of not less than five (5) percent in the credit tranches sold or transferred to the investors or in a representative sample of the securitized financial assets equal to not less than five (5) percent of the principal amount of the financial assets at transfer." FDIC Proposing Release, 75 Fed. Reg. at 27485. In making this change, the FDIC was responding to concerns that the risk retention requirement "could cause securitizations that might otherwise qualify for sale accounting treatment under the 2009 GAAP Modifications to not qualify for that treatment." Id. at 27479. By requiring a retention of risk in the assets securitized, rather than in securities of the securitization entity itself, the FDIC would mitigate the consequences of the retained risk requirement for GAAP accounting consolidation. The Commission should consider a similar amendment to the Proposed Rules.

4. The Commission should clarify Rule 430D(d)(2)

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[17] Other than the final catchall clause, this list of types of Swaps is taken from the Dodd-Frank Act definition of "Swap," excluding credit-related derivatives that it would appear the Commission intends to treat as "structured finance products."

[18] This is the definition added by section 721(47) of the Dodd-Frank Act.

[19] Section 941 of the Dodd-Frank Act.

Rule 430D(d)(2) as proposed specifies that "[i]nformation omitted from a form of prospectus that is part of an effective registration statement in reliance on paragraph (a) of this section that adds a new structural feature or credit enhancement must be included subsequently in the prospectus that is part of a registration statement by a post-effective amendment to the registration statement." Proposing Release, 75 Fed. Reg. at 23437. We have two concerns with the proposed language. First, a post-effective amendment should be prompted by information that is not only new, but materially different. The Commission should consider revising the rule to refer to "a new structural feature or credit enhancement materially different from any of the alternative structural features or credit enhancements specified in such form of prospectus." Second, the Commission should address a possible misconstruction of the rule. The Commission's intent seems clearly to be that "assets, structuring and other features may be presented in brackets in the form of prospectus filed with the registration statement" and "issuers could include the same bracketed information in the form of prospectus filed with the registration statement." Proposing Release, 75 Fed. Reg. at 23353. Rule 430D(d)(2), however, could be construed to require a post-effective amendment merely to give effect to the *election among* alternative structural features or credit enhancements, since the information regarding the choice among such features is not in fact set out in the initial form of prospectus, or may change during the course of an offering, and in some circumstances might be thought "new." The Commission should specify for clarity that information indicating the election among structural features or credit enhancements described in the initial form of prospectus, or the change from one such structural feature or credit enhancement to an alternative structural feature or credit enhancement also described in the initial form of prospectus, does not require a post-effective amendment.

5. Ongoing reporting required after termination of Exchange Act reporting requirements should be subject to an investor opt-out.

The importance of reporting in an ABS transaction is greatest to investors in the earlier years a security is outstanding. We acknowledge the Commission's well-articulated concern that adequate information should continue to be available in relation to ABS even after the minimum period for public reporting imposed by Section 15(d) under the Exchange Act. Nevertheless, the performance of securitized portfolios is heavily influenced by the quality of underwriting, and would rarely be expected to change dramatically in the later years a security is outstanding. At the same time, for an issuer of ABS to continue transaction reporting even when the portfolio is well seasoned, and the principal balance of the outstanding securities and the assets held by the issuer are greatly reduced, may be nearly as expensive as the reporting in the earlier years of the transaction. If the direct obligation of an issuer to make ongoing reporting under the Exchange Act has terminated, it may well be the case that investors in the transaction would desire to terminate some aspects of continued reporting in return for recovering the attendant costs. Investors ought to be given this option. Thus, the Commission should provide, for purposes of the undertaking in new Item 512(a)(7) of Regulation S-K, that after a minimum period of time a transaction has been outstanding, investors in the transaction may by a specified vote terminate the obligations of the issuer for continued reporting.

6. The Commission should grandfather certain resecuritizations of existing ABS

As noted above, the basic contract as to the type and extent of information that is obtainable in connection with a structured finance transaction is largely fixed at the time of issuance of the relevant securities. Therefore, most secondary purchasers of structured finance securities, if they attempt to effect a resecuritization of such securities, will be unable to comply with the Commission's specification that they "[p]rovide asset-level information . . . for the assets backing those ABS." Proposing Release, 75 Fed. Reg. at 23428. This will be a barrier not only to a public resecuritization of ABS, but to any Rule 144A resecuritization as well, because there will be no way to ensure the availability of such information to subsequent holders of the resecuritization interests. While the Commission's goal of improving the quality of ABS information and disclosure no doubt dictates that resecuritizations be addressed, the Proposed Rules would make practically impossible resecuritization transactions that could otherwise provide badly needed liquidity for outstanding Rule 144A structured finance securities. The Commission should consider grandfathering all Rule 144A "structured finance products" for purposes of Rule 144A resecuritizations that are themselves eligible for Rule 144A, by providing that the "look through" standard of Item 11 of Schedule L does not apply to a Rule 144A resecuritization of a "structured finance product" security outstanding prior to the effective date of the Proposed Rules. If this broad an exemption is not acceptable, the Commission should consider such an exemption in relation to a "structured finance product" that does not represent more than a specified portion, such as 20%, of a particular resecuritization. The Proposed Rules should not indirectly penalize holders of existing 144A structured finance securities by cutting off one avenue for the resale of such securities.

7. <u>The Commission should reframe Rule 192</u>.

Proposed Rule 192 specifies that where information is required to be provided in accordance with a Rule 144A, Regulation D or Rule 144 undertaking, a failure to provide such information "would constitute an engagement in a transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser of the securities." Proposing Release 75 Fed. Reg. at 23436. The Commission should recognize the fundamental and longstanding distinction between a covenant and a representation, between simple inaction and deceit. We agree with the Commission's articulated concern that "a potential claim arising under Section 5 of the Securities Act may not be the appropriate remedy under these circumstances but believe it appropriate that there be regulatory consequences." <u>Id</u>. at 23397. Nevertheless, it would appear that an effective penalty provision could be linked to a breach of undertakings to the Commission, and be incurred only if an investor complaint is not appropriately addressed by the issuer or sponsor. It does not seem necessary or appropriate that a failure to meet a reporting obligation be characterized as a "fraud or deceit," unless the Commission can establish that the issuer or sponsor acted in bad faith in that it never intended to comply with the information furnishing undertaking.

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We would be pleased to respond to any inquiries regarding this letter or our views on the Proposed Rules generally. Please contact Leslie N. Silverman at 212-225-2380, Raymond B. Check at 212-225-2122 or Michael A. Mazzuchi at 202-974-1572.

Very truly yours,

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