July 15, 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 Number S7-08-10)[1]

Dear Ms. Murphy:

The Council of Institutional Investors ("Council") welcomes the opportunity to comment on the Securities and Exchange Commission's ("SEC" or "Commission") April 7, 2010 release *Asset-Backed Securities* ("Proposed Rule" or "Release"). As a leading voice for long-term investors, the Council represents public, corporate, and union pension funds with combined assets over $3 trillion. Significantly affected by the global financial crisis, our member funds have a deep interest in addressing the flaws in the market for asset-backed securities ("ABS") that contributed to and exacerbated the recent crisis.

Consistent with the findings and recommendations of the blue-ribbon Investors' Working Group ("IWG"), [2] we believe the proposed revisions to Regulation AB and other rules regarding the offering process, disclosure and reporting for ABS will help address some of the problems plaguing this important market—namely, poor information and an overreliance on credit ratings. The Council accordingly supports the Release.

Enhancing ABS Disclosures

Financial markets require timely and reliable information to properly allocate capital and price risk. Current rules regarding ABS, however, "provide for woefully inadequate disclosures to potential investors in these products."[3] "Investors have had a difficult time understanding securitized instruments," the IWG found, "because of the lack of information about them and the confusing manner in which this information is reported."[4] As a result, investors in securitized products "lack crucial information needed to judge their true risk."[5]

Whatever the causes of the securitization market's recent drift from economic fundamentals, poor disclosures undoubtedly allowed this gap to widen and persist. In addition, inadequate information deepened the pain of the market's inevitable adjustment. As investors struggled to price troubled securities amid the financial crisis, massive uncertainty surrounding the value of so-called "toxic" assets intensified the market panic. With better disclosures, much of this uncertainty may have been avoided. Improving ABS transparency is accordingly a core recommendation of the IWG.

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[1] Asset-Backed Securities, 75 Fed. Reg. 23328 (proposed Apr. 7, 2010) (to be codified at 17 CFR pts. 200, 229, 230, 232, 239, 240, 243, and 249), *available at* http://www.sec.gov/rules/proposed/2010/33-9117fr.pdf.
[2] Investors' Working Group, U.S. Financial Regulatory Reform: The Investors' Perspective (July 2009), *available at* http://www.cii.org/UserFiles/file/IWGreport.pdf. The Council fully endorsed the recommendations of the IWG in fall 2009. For more information, please visit http://www.cii.org/iwgInfo.
[3] *Id.* at 14.
[4] *Id.* at 12.
[5] *Id.* at 13.

In order to address the dangerous opacity in the securitization market, the IWG proposed that the SEC "require sponsors of asset-backed securities to improve the timeliness and quality of disclosures to investors in these instruments and other structured products."[6] Consistent with the panel's findings that investors are often denied "a reasonable opportunity to review disclosures before making a decision to invest," we believe the Commission is correct to conclude that investors need additional time to review information on a particular shelf takedown in advance of the first sale of securities in the offering.[7] The Council overall agrees with the IWG that a special regulatory framework is needed for ABS shelf offerings:

> Because each ABS offering involves a new and unique security, the IWG does not believe the SEC should allow such issuances to be eligible for its normal shelf-registration procedures. Instead, the SEC should develop a regulatory regime for such asset-backed securities that would require issuers to make prospectuses available for potential investors in advance of their purchasing decisions. These prospectuses should disclose important information about the securities, including the terms of the offering, information about the sponsor, the issuer and the trust, and details about the collateral supporting the securities. Such new rules would give investors critical information they need to perform due diligence on offerings prior to investing.[8]

Taken as a whole, the Proposed Rule is largely consistent with this recommendation. Comprehensive asset level disclosures available electronically along with a computer program simulating the payments "waterfall" will significantly enhance investors' understanding of often extremely complex securitized products. Ongoing reporting requirements will keep markets better informed as conditions change. Information about the history, incentives, and financial condition of ABS originators and sponsors will also help investors more accurately judge the reliability of these important intermediaries. Since the IWG's recommendations encompass ABS "and other structured products," the Council supports requiring issuers in private securitization markets to provide similar disclosures to investors upon request.[9]

Reducing Reliance on Credit Ratings

Besides a lack of critical information, investors' overdependence on deeply flawed credit ratings issued by Nationally Recognized Statistical Rating Organizations ("NRSROs") additionally fostered severe ABS misvaluations. "Well into the credit crisis," the IWG noted, "NRSROs maintained triple-A ratings on complex structured financial instruments despite the poor and deteriorating quality of the sub-prime assets underlying those securities."[10] As the financial crisis painfully revealed, many credit ratings clearly proved less than reliable. Unfortunately, as the IWG concluded, "Many institutional investors have come to rely on credit rating agencies as a basic investment screen, a problem that is exacerbated by the lack of adequate disclosures in the sale of asset-backed securities."[11]

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[6] *Id.* at 14.
[7] *Id.* at 12.
[8] *Id.* at 14.
[9] *Id.*
[10] *Id.* at 20.
[11] *Id.* at 19.

This reliance, however, was in turn promoted by regulatory dependence on NRSRO ratings—such as the investment grade standard for shelf eligibility—which encouraged investors "to put more faith in the rating agencies than they should."[12] The IWG consequently recommended that "Reliance on NRSRO ratings should be greatly reduced by statutory and regulatory amendments."[13] The Council accordingly supports provisions in the Proposed Rule designed to reduce reliance on NRSRO ratings and promote greater due diligence by investors. Replacing the ABS investment grade rating standard for delayed shelf registration with criteria more directly related to the character and quality of securitized products should help achieve this goal.

The Council believes a commitment by ABS issuers to provide ongoing reporting is an appropriate criterion for ABS shelf eligibility. Transparency is certainly related to asset quality. Reliable disclosures may promote liquidity, for example, particularly during periods of market turbulence and stress. A commitment to ongoing disclosures might also be an indicator of an issuer's confidence in the quality of the assets. Finally, ongoing reporting will facilitate continued due diligence by investors beyond the initial decision to participate in an ABS offering.

Faced with minimal disclosure requirements and often insufficient scrutiny from credit raters and investors, ABS issuers demonstrated little incentive to focus on asset quality. In order to address this costly disconnect, the Council supports an additional risk retention standard for shelf eligibility. Explicitly endorsed by the IWG, "Having 'skin in the game' would make sponsors more thoughtful about the quality of the assets they securitize."[14] While this requirement will be implemented by Sec. 941 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act*,[15] we nevertheless agree with the Commission that risk retention is a meaningful indicator of asset quality and thus an appropriate criterion for ABS shelf registration.

Conclusion

The Council of Institutional Investors appreciates the opportunity to comment. We support the Proposed Rule as we believe that the various changes overall will help address some of the serious flaws in the market for asset-backed securities revealed by the financial crisis. If you have any questions about our views, please do not hesitate to contact me at (202) 261-7096 or jonathan@cii.org, or our general counsel Jeff Mahoney at (202) 261-7081 or jeff@cii.org.

Sincerely,

Jonathan D. Urick

Jonathan D. Urick
Analyst
Council of Institutional Investors

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[12] *Id.* at 20.
[13] *Id.* at 21.
[14] *Id.* at 14.
[15] H.R. Rep. No. 111-517, at 524 (2010) (Conf. Rep.), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_reports&docid=f:hr517.111.pdf.