

## MEMORANDUM

**To:** Commission File No. S7-08-10

**From:** Rolaine S. Bancroft  
Attorney-Advisor  
Office of Rulemaking  
Division of Corporation Finance  
U.S. Securities and Exchange Commission

**Date:** July 27, 2010

**Re:** Proposing Release on Asset-Backed Securities (Release Nos. 33-9117; 34-61858)

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On July 22, 2010, Paula Dubberly, Katherine Hsu, Rolaine Bancroft, Eduardo Aleman, and Jay Knight of the Division of Corporation Finance and Eric Emre Carr and Stanislava Nikolova of the Division of Risk, Strategy and Financial Innovation met with representatives of Ford Credit. Among the topics discussed was the Commission's April 7, 2010 proposing release regarding asset-backed securities. Handouts are attached to this memorandum.

Attachment



**FordCredit**

***OVERVIEW OF  
FORD CREDIT BUSINESS  
AND SECURITIZATION PROGRAMS***

***JULY 22, 2010***

# ***FORD CREDIT SECURITIZATION TEAM***

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# ***FORD CREDIT GOALS***

- **Provide an overview of our:**
  - **Business model**
  - **Asset classes we securitize**
- **Discuss the risk management principles that Ford Credit uses to manage its business and ensure prudent underwriting and collections**
- **Explain how Ford Credit has always had skin in the game and aligned incentives with investors**

# **FORD CREDIT AGENDA**

- |    |                                   |    |
|----|-----------------------------------|----|
| 1. | Overview                          | 4  |
| 2. | Assets, Origination and Servicing | 8  |
| 3. | Securitization Overview           | 22 |

## ***FORD CREDIT INTRODUCTION***

- **Ford indirectly owns 100% of Ford Credit**
- **Ford Credit has over 50 years of experience in the auto financing business, financing Ford dealers and vehicle sales**
- **Ford Credit offers a wide variety of automotive financing products to and through automotive dealers around the world**
- **In the U.S., as of year-end 2009, Ford Credit was financing:**
  - **Over 3,100 Ford dealers (about 80%)**
  - **Over 2.5 million retail loan customers**
  - **Over 650,000 retail lease customers**

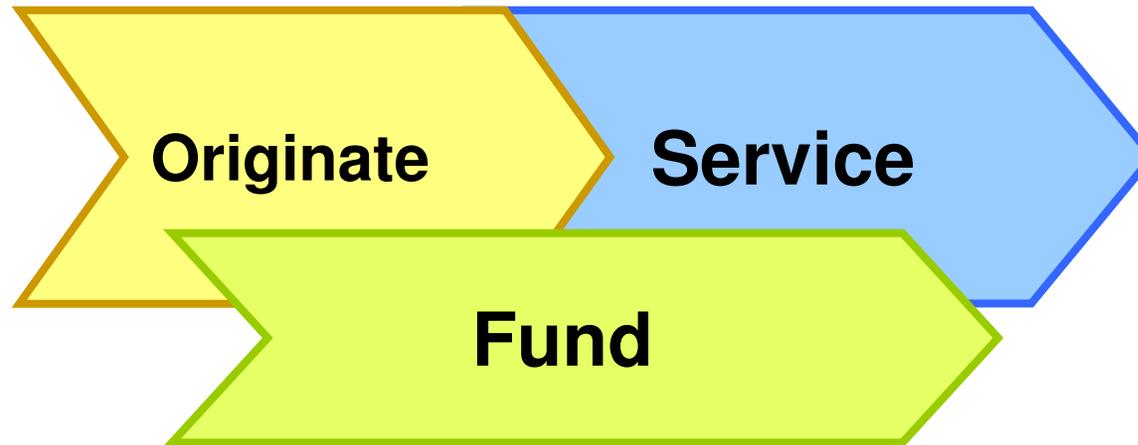
**Ford views Ford Credit as a long term strategic asset whose mission is to profitably and consistently support the sale of Ford vehicles around the world**

**FORD CREDIT**  
**BALANCE SHEET**

|                           | <b>Year-end<br/><u>2009</u><br/>(Bils.)</b> |
|---------------------------|---|
| <b><u>U.S. Assets</u></b> |   |
| Retail Loans              | \$ 36.3                                     |
| Retail Leases             | 11.4  |
| Floorplan Loans           | 12.3  |
| Other                     | 3.0   |
| Subtotal U.S.             | \$ <u>63.0</u>                              |
| <br><b><u>Other</u></b>   |   |
| International Assets      | 34.4  |
| Reserves and Other        | <u>(2.9)</u>                                |
| Total Global Assets       | \$ <u><u>94.5</u></u>                       |

# **FORD CREDIT BUSINESS MODEL**

- Buy it Right
- Collect it Effectively
- Operate Efficiently



- Fund it Efficiently
- Manage Balance Sheet Risk
- Purchase managed level of risk, eliminating highest risks through prudent origination practices
- Collect using the latest technology and consistent processes which are continually improved
- Fund assets efficiently through unsecured and securitization markets

# **FORD CREDIT AGENDA**

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## ***FORD CREDIT RETAIL LOANS BACKGROUND***

- **Ford Credit finances about half of Ford's U.S. retail sales -- about 75-85% of which are retail loans and 15-25% are retail leases**
- **Our retail loans are “plain vanilla”, fixed rate, simple interest contracts with level monthly payments and original terms of 72 months or less**
- **Originating “plain vanilla” retail loans has been our practice for decades. Consistent origination policies have allowed us to develop a deep history of loan performance throughout economic cycles**
- **This historical data is an extremely valuable company asset and key source of competitive advantage**

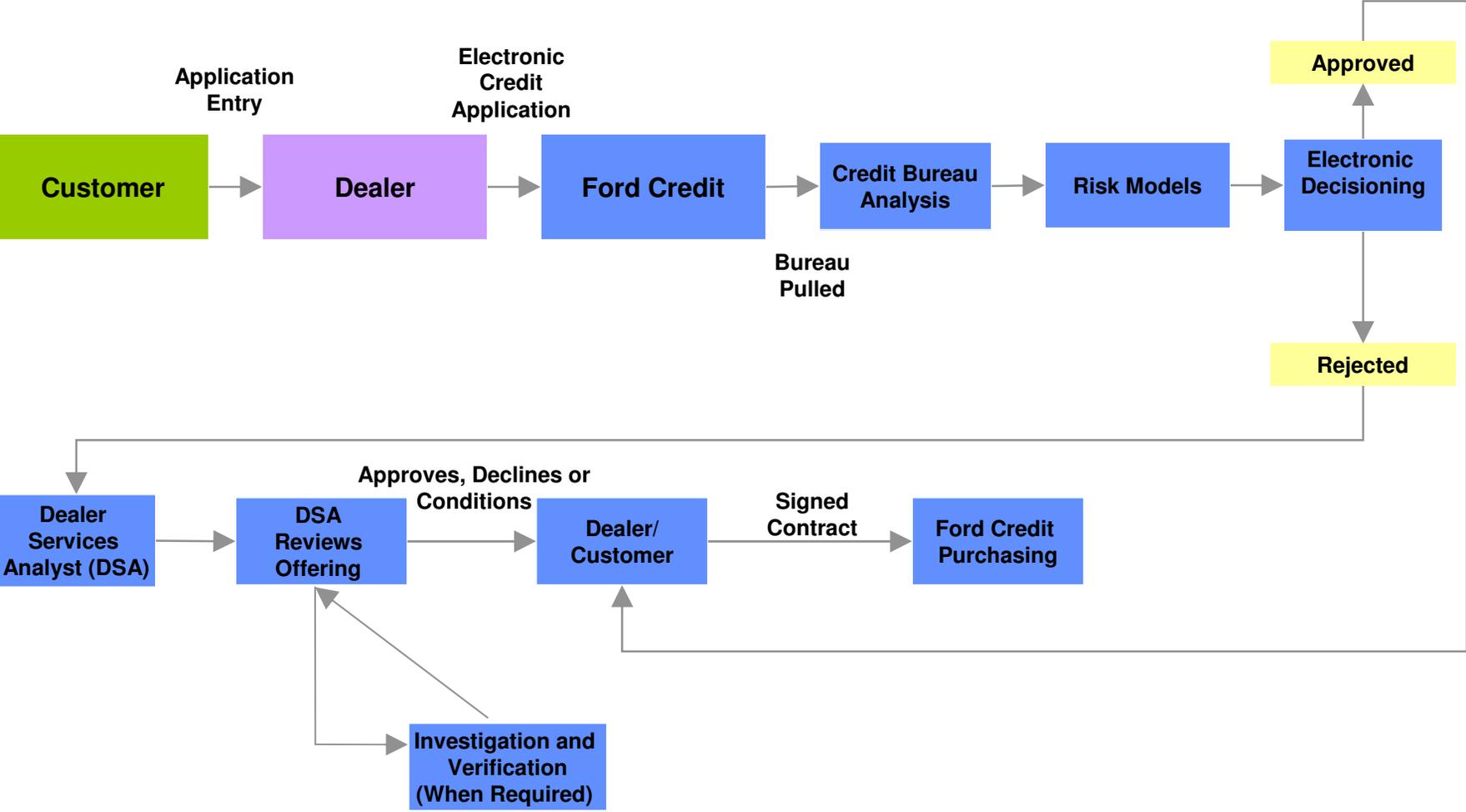
## ***FORD CREDIT RETAIL LOAN PURCHASE POLICY***

- **Ford Credit's retail loan portfolio is considered "prime", with a weighted average FICO® score in excess of 700**
  - **We leverage our experience and expertise in the auto finance business to purchase loans across the entire risk spectrum**
  - **We maintain a consistent proportion of higher- to lower-risk customers (as measured by FICO®)**
  - **Our ability to provide financing to the entire risk spectrum of customers has been important given inconsistent support from other finance providers, especially at the bottom of an economic cycle**

***FORD CREDIT  
RETAIL LOANS – ORIGINATIONS PROCESS***

- **Ford Credit is an indirect lender**
- **Dealer and customer negotiate the financed amount, payment terms and interest rate to be charged on the retail loan subject to Ford Credit's approval**
- **Dealer submits a credit application and loan terms to Ford Credit and/or other lenders, who will either approve, decline or condition the purchase of the loan from the dealer**
- **Ford Credit purchases the loan from the dealer at the rate and terms negotiated by the dealer and the customer and approved by Ford Credit**

# FORD CREDIT RETAIL ORIGINATIONS PROCESS DIAGRAM



# ***FORD CREDIT***

## ***RETAIL LOAN ORIGINATION AND SERVICING***

- **Ford Credit uses proprietary scoring models that emphasize the customer's creditworthiness and ability to pay**
- **Our scoring models consider:**
  - **FICO® score**
  - **Financing product (retail, lease)**
  - **Customer characteristics (payment-to-income)**
  - **Contract characteristics (loan-to-value, term, payment)**
- **Ford Credit is a best-in-class servicing organization**
- **Credit losses are an expected part of the business -- the objective is to implement consistent and prudent origination and collection strategies to ensure the loans perform as expected**
- **Our collection strategy is to:**
  - **Reduce credit losses**
  - **Optimize utilization of resources**
  - **Increase customer satisfaction**

## ***FORD CREDIT RETAIL LEASE BACKGROUND***

- **Leasing provides our customers with an alternative to a traditional retail loan and is another way that Ford Credit supports the sale of new Ford cars and trucks**
- **Our retail leases are “plain vanilla”, fixed payment, new vehicle contracts for a period of 48 months or less. At the end of the lease term the customer can either purchase the vehicle or return it to Ford Credit**
- **Ford Credit sells returned vehicles at used car auctions**
- **In simple terms, a lease is a stream of monthly rental payments with a large payment at the end (at the customer’s option), representing the residual value of the vehicle (its value as a used vehicle)**
- **Ford Credit is Ford’s primary consumer lease financing provider**

**FORD CREDIT**  
**RETAIL LEASE ORIGINATION AND SERVICING**

- **Origination and servicing processes are the same as retail loans**
- **Lease customers are generally more creditworthy**
- **Residual risks managed through:**
  - **Use of proprietary models to set residual values**
  - **Appropriate vehicle model concentrations**
  - **Smoothing of lease maturities**
  - **Geographic distribution of auction sales to maximize proceeds**

## ***FORD CREDIT FLOORPLAN FINANCING BACKGROUND***

- **Floorplan financing is a cornerstone product for Ford Credit**
- **Floorplan financing builds dealer satisfaction, which, together with our retail loan and retail lease purchase policy, strengthens long-term relationships with our dealers**
- **Ford Credit finances about 3,100, or 80%, of Ford's U.S. dealers**
- **When the economy and credit markets are strong, banks have historically competed for floorplan business, but are quick to pull back from this business during an economic downturn**

## ***FORD CREDIT FLOORPLAN ORIGINATION***

- **Floorplan financing is important as it allows dealers to purchase their vehicle inventory from Ford**
- **Floorplan financing is revolving and each loan is secured by a specific purchased vehicle**
- **A floorplan loan is repaid when the dealer sells or leases the vehicle to a customer, typically 60-75 days after the vehicle is purchased by the dealer**
- **Dealers wishing to establish a floorplan credit line must undergo a thorough credit review focused on:**
  - **Capitalization and leverage**
  - **Cash flow**
  - **Profitability**
  - **Credit history**

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## ***FORD CREDIT FLOORPLAN -- DEALER RISK RATING***

- **We use proprietary credit scoring models to assign a risk rating to each dealer**
- **Based on our proprietary credit scores, we assign dealers to the following groups:**
  - **Group I – Strong to superior**
  - **Group II – Fair to favorable**
  - **Group III – Marginal to weak**
  - **Group IV – Poor to uncollectible**
- **These groups are used in our floorplan business and determine the extent and frequency of dealers and credit line monitoring**
- **Dealer monitoring focuses on:**
  - **Size and trends of outstanding amount financed**
  - **Payoff verification**
  - **Inventory aging**
  - **Financial condition**

# **FORD CREDIT ORIGINATION AND SERVICING**



**Technology and judgment combine to minimize losses**

## ***FORD CREDIT***

# ***SUMMARY OF RISK MANAGEMENT***

- **Ford Credit's best-in-class risk-adjusted loss performance is a result of its origination and servicing strategies and competencies**
- **We purchase a managed level of risk**
  - **Proprietary statistical models assess risk and drive collection strategies**
  - **The highest risks are eliminated through prudent origination practices**
- **Our collection strategy focuses on:**
  - **Reducing credit losses**
  - **Optimizing the utilization of resources**
  - **Increasing customer satisfaction**
  - **Utilizing technology and processes which are continually improved**
- **The data and experience from financing tens of millions of contracts over 50 years is a strategic asset that increases our competitiveness**

**Historical data has been critical to our  
origination and servicing success**

# ***FORD CREDIT AGENDA***

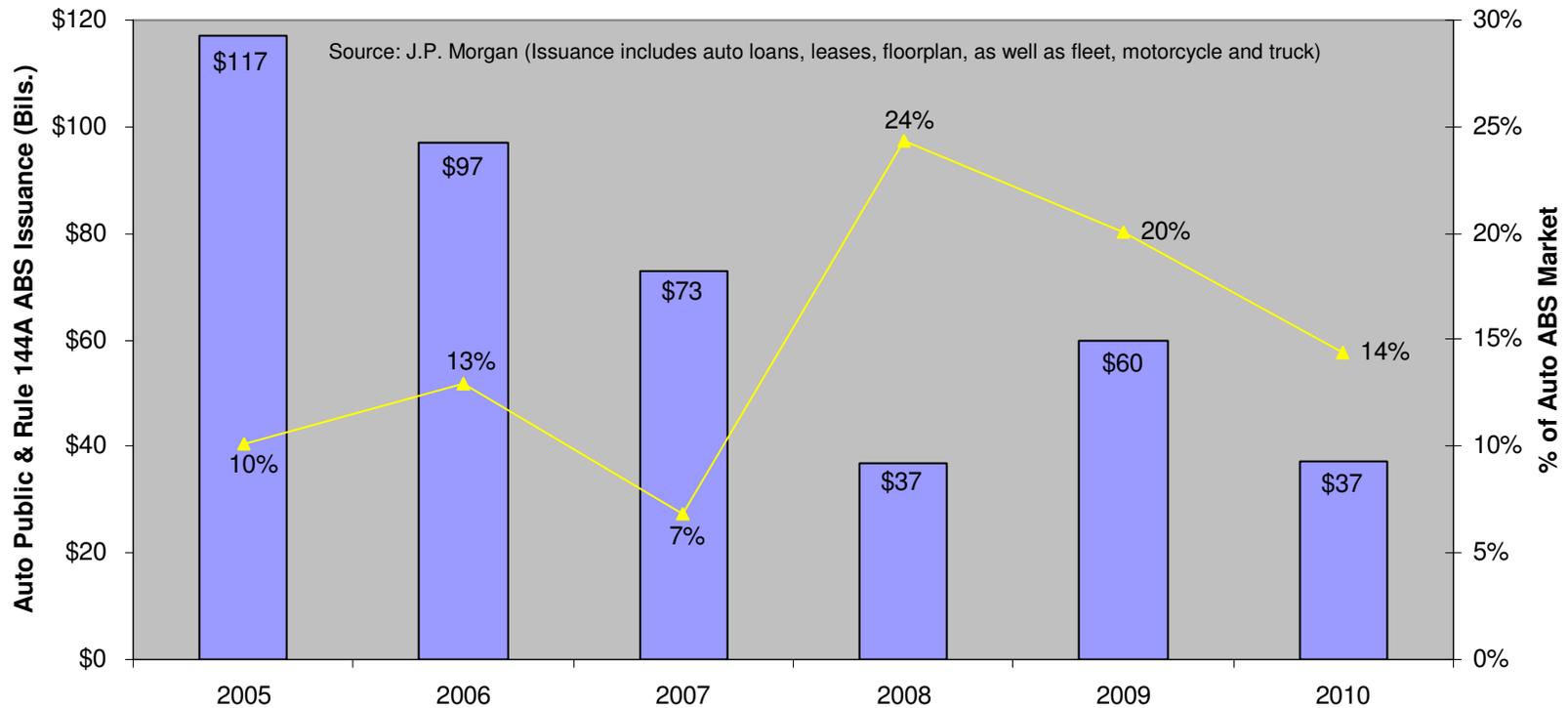
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## ***FORD CREDIT SECURITIZATION STRATEGY AND HISTORY***

- **Earlier this decade, securitization funding was more expensive than unsecured debt, but was pursued to diversify our funding**
- **Since we lost our investment grade rating in 2005, securitization funding has been critical to Ford Credit's liquidity (almost 60% of our overall funding) and has been very cost-effective**
- **Ford Credit has a long securitization history**
  - **Retail loan program began in 1989**
  - **Floorplan program began in 1992**
  - **Lease program began in 1995**

# FORD CREDIT

## OUR ISSUANCE AND % OF AUTO ABS MARKET



Memo (\$Bils):  
 Ford Credit  
 Public and Rule  
 144A Issuance

|        |        |       |       |        |       |
|--------|--------|-------|-------|--------|-------|
| 2005   | 2006   | 2007  | 2008  | 2009   | 2010  |
| \$11.8 | \$12.6 | \$5.0 | \$9.0 | \$12.1 | \$5.3 |

**Ford Credit has consistently been a major ABS market participant and since the crisis we have been a larger percentage of the market**

## ***FORD CREDIT***

### ***IMPORTANCE OF REPUTATION***

- **Our capital markets reputation is very important**
- **Our business model and securitization programs ensure consistent alignment with investors**
  - **We do not use the originate to distribute model**
  - **We are the originator, sponsor, servicer and equity holder in our transactions**
  - **We do not use securitization to transfer risk or to achieve off-balance sheet accounting treatment**
  - **We hold significant amounts of unsecuritized retail loans on our balance sheet**
  - **We have incentives for long-term relationships with investors, rating agencies, customers and underwriters**
- **We focus on what we know how to do well -- prudent underwriting of auto financing. Ford Credit has no residential mortgages**
- **We use a clean and transparent offering process. All disclosures contained in preliminary prospectus (other than pricing) -- no changes made between offering and settlement**

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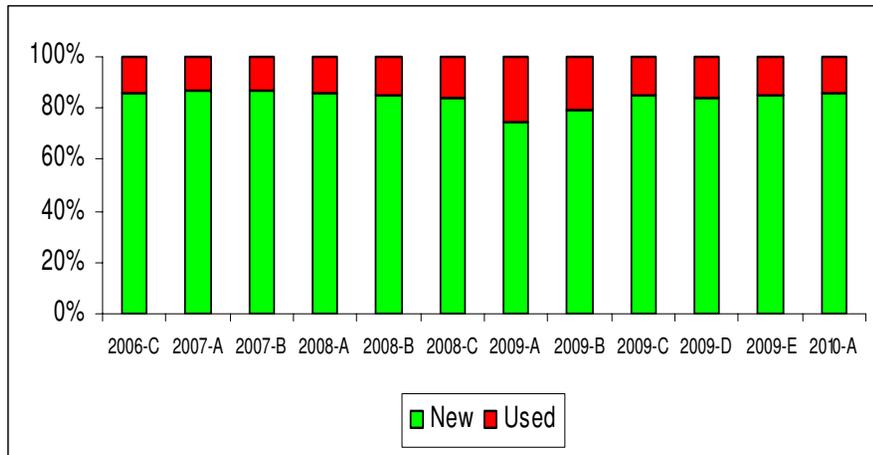
## ***FORD CREDIT***

# ***KEY CHARACTERISTICS OF AUTO COLLATERAL***

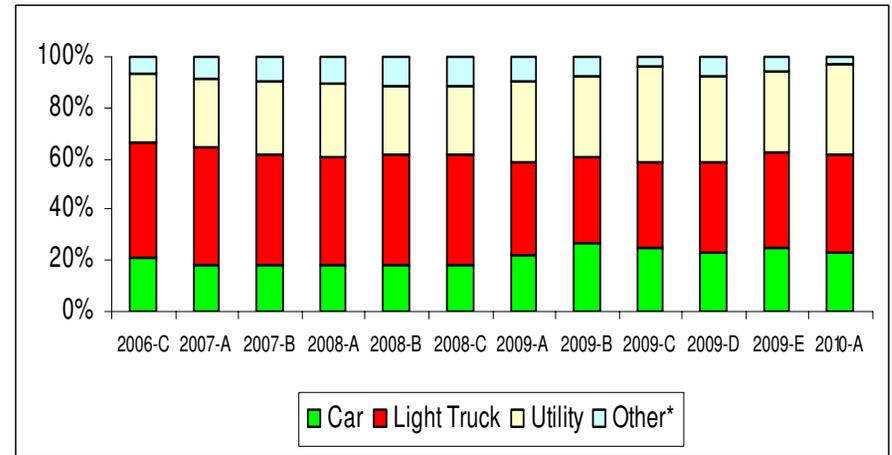
- **Cars and light trucks are reliable collateral:**
  - They are depreciating assets so they are not subject to speculation
  - Highly efficient used car and auction markets make them very liquid
- **Auto ABS has historically performed well, even during the crisis, despite:**
  - Worst economic recession since the Great Depression
  - High unemployment
  - Worst auto industry sales in recent history
  - Bankruptcy of major auto manufacturers
  - Record high gasoline prices that caused used vehicle prices to decline

# FORD CREDIT RETAIL ABS COLLATERAL COMPOSITION

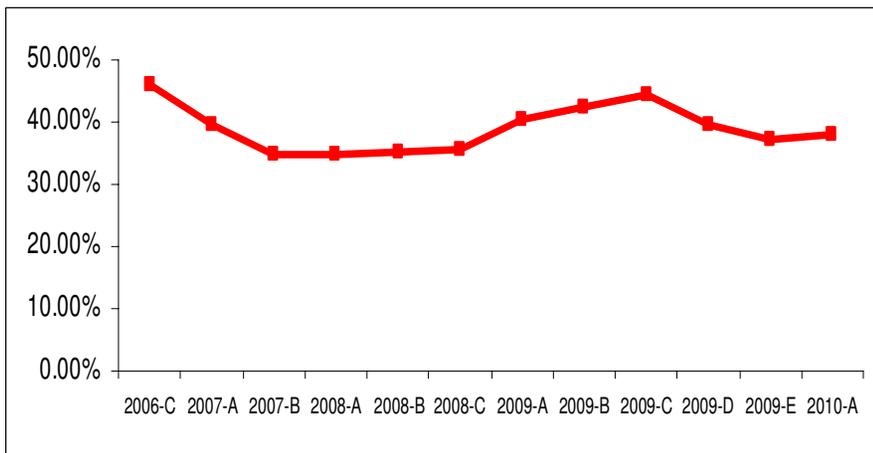
### New/Used



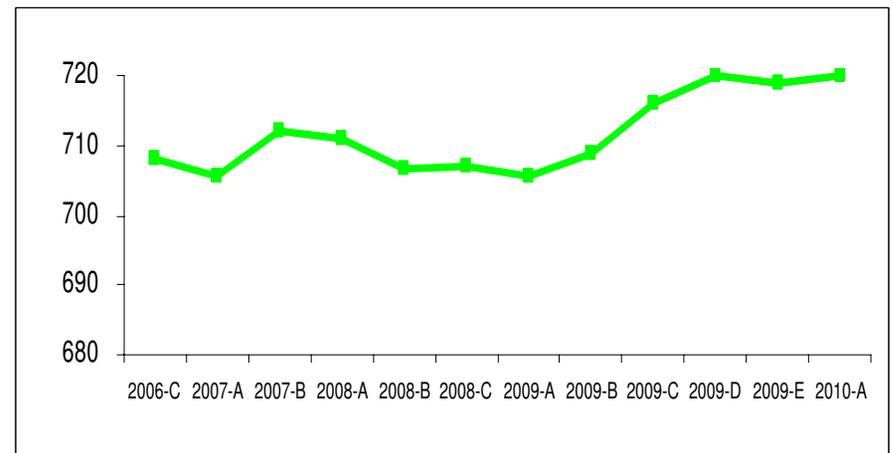
### Car/Light Truck/Utility



### % of Contracts > 60 month original term



### Weighted Average FICO



\* Primarily non-Ford, Lincoln and Mercury vehicles, which Ford Credit does not categorize

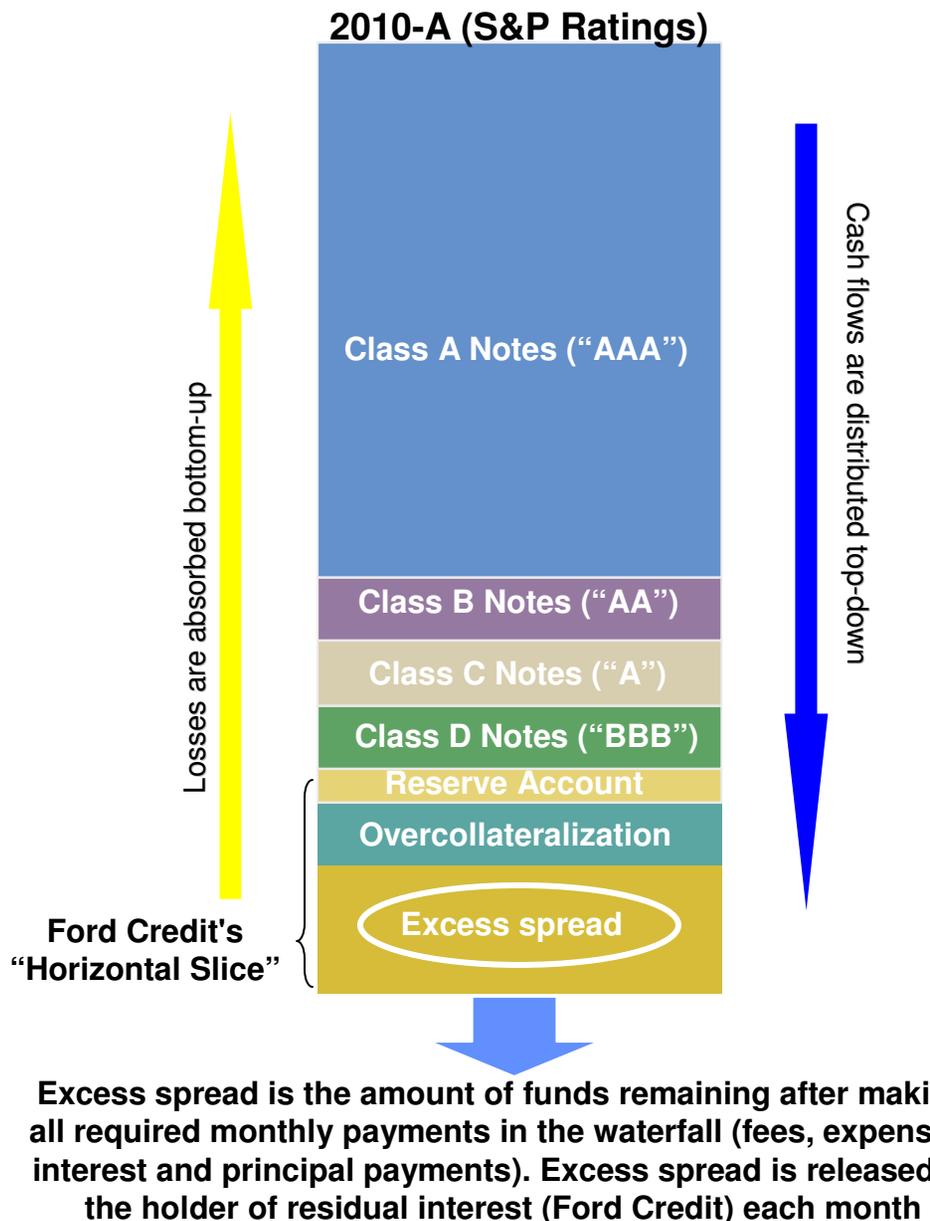
***FORD CREDIT***  
***RETAIL ABS COLLATERAL COMPOSITION***

- **Consistent origination and servicing practices lead to predictable portfolio composition**
- **Ford Credit selects a cross-section of retail loans from our portfolio for each securitized pool**
- **Pools have reflected trends in the industry and in our business**
- **Superior loss and delinquency trends for both our portfolio and securitized pools compared to many of our competitors**

## ***FORD CREDIT RETAIL TRANSACTION STRUCTURE***

- **Credit enhancements in our retail loan securitization programs are:**
  - **Cash reserve**
  - **Subordination of junior notes**
  - **Overcollateralization (including residual interest in trust)**
  - **Excess spread**
- **Total enhancement for AAA rated Class A Notes typically exceeds 7%**
- **Transactions structured to build credit enhancement over time**
- **Conservative structure is designed for investor, agency and underwriter comfort**
- **Senior/subordinate, sequential pay structure**
- **Consistent structure for more than fifteen years**

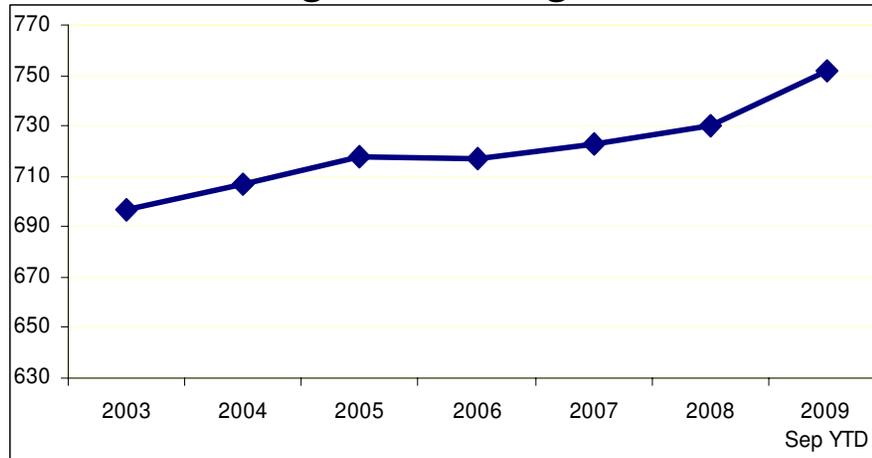
# FORD CREDIT RETAIL SECURITIZATION CREDIT ENHANCEMENT



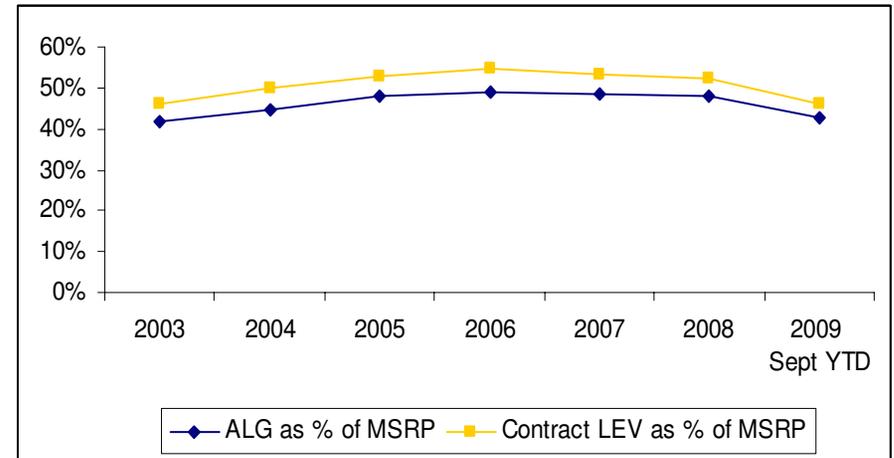
- Credit enhancement provides protection against payment shortfalls resulting from losses on securitized pool of retail loans
- Rating agency loss expectations and stress scenarios determine required enhancement levels
- Typically, a AAA rating requires enhancement that provides at least five times expected loss coverage
- Class A Notes have the full support of all the credit enhancement in the form of:
  - Hard credit enhancement
    - Overcollateralization (builds to target)
    - Non-declining reserve account
    - Subordination of Class B,C,D notes
  - Soft credit enhancement
    - Excess spread
- Losses on retail loans in each period are absorbed in the following order:
  - 1st loss position = Excess spread
  - 2nd loss position = Overcollateralization
  - 3rd loss position = Reserve account
  - 4th loss position = Class D notes
  - 5th loss position = Class C notes
  - 6th loss position = Class B notes

# FORD CREDIT LEASE PORTFOLIO ORIGINATION COMPOSITION

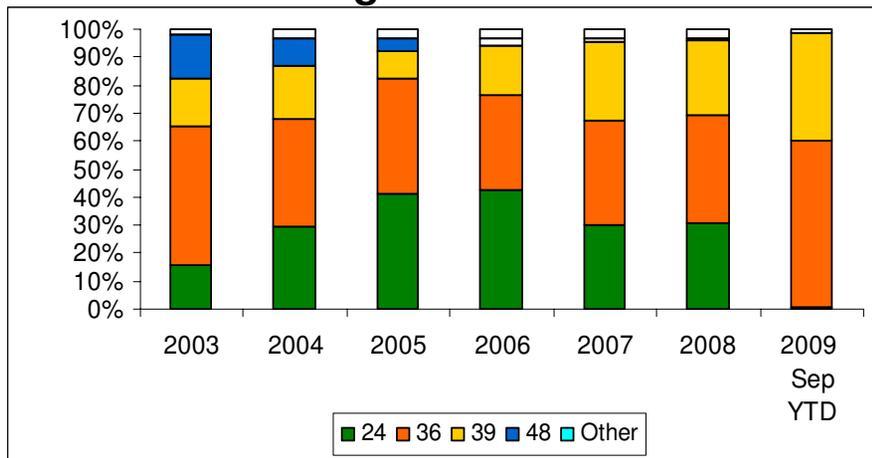
### Weighted Average FICO



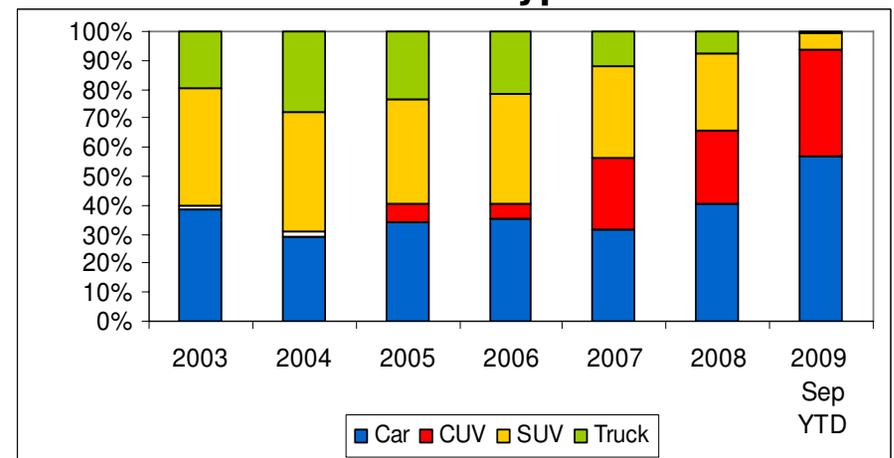
### Residual Values



### Original Term



### Vehicle Type



Data Based on Year of Origination

## ***FORD CREDIT LEASE SECURITIZATION OVERVIEW***

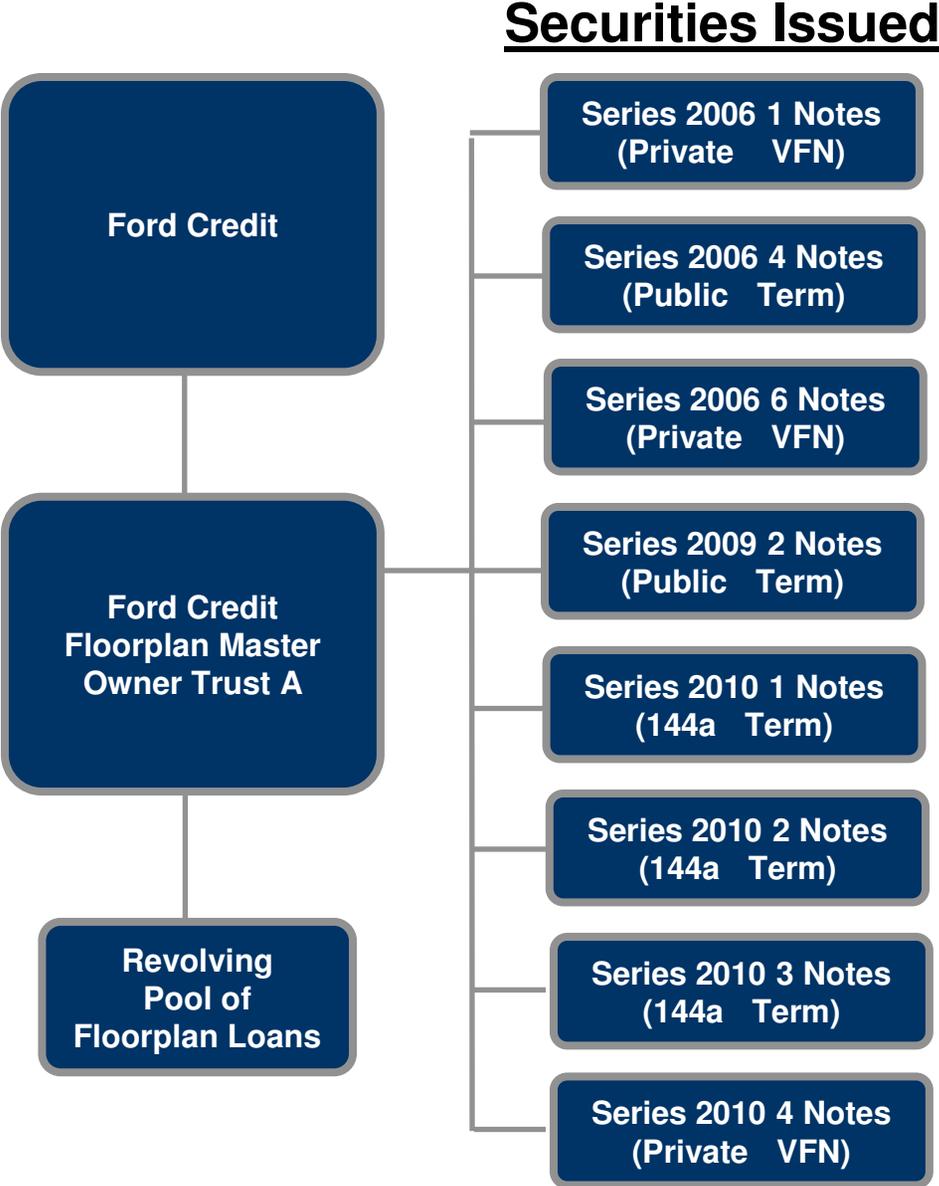
- **Ford Credit has extensive experience in lease securitizations**
- **Lease securitizations have been executed through multiple channels, including:**
  - **Private transactions**
  - **Bank-sponsored commercial paper conduits**
  - **Rule 144A transactions**
- **Similar to retail loan securitizations, Ford Credit selects a cross-section of leases from our portfolio for each securitized pool**
- **Consistent origination and servicing practices lead to predictable portfolio composition and credit loss trends**

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## ***FORD CREDIT LEASE TRANSACTION STRUCTURE***

- **Credit enhancements in our lease securitization programs are:**
  - **Cash reserve**
  - **Subordination of junior notes**
  - **Overcollateralization (including residual interest in trust)**
  - **Excess spread**
- **Higher levels of enhancement required due to residual value risk. For any vehicle returned at the end of the lease, the transaction bears the risk that the vehicle will be worth less than the value projected at the beginning of the lease**
- **Transactions are structured to build enhancement over time**
- **Conservative structure is designed for investor, agency, and underwriter comfort, and is based on AAA criteria:**
  - **5 times credit loss coverage**
  - **Residual losses are estimated assuming all vehicles (other than defaults) are returned and sold for 55-60% of their projected residual values**
- **Senior/subordinate, sequential pay structure**

# FORD CREDIT FLOORPLAN STRUCTURE



## ***FORD CREDIT FLOORPLAN OVERVIEW***

- **Master trust owns a revolving pool of floorplan loans originated in connection with the purchase and financing by motor vehicle dealers of their new and used car and truck inventory**
- **At any time, the master trust owns approximately 400,000 floorplan loans that are repaid on average after 60-75 days**
- **Master trust issues new series of asset-backed securities from time to time that are all backed by the same pool of floorplan loans**
- **Typically, principal on the securities is paid in a lump sum at maturity**
- **Variable funding notes are used to adjust the balance of issued securities to match the balance of floorplan loans owned by the master trust**

**Due to the revolving nature of the pool of floorplan loans, the transactions require very different structures and disclosures compared to retail and lease**

## ***FORD CREDIT FLOORPLAN STRUCTURE***

- **Rating agencies model potential losses by predicting the number of dealer defaults, timing of dealer defaults and vehicle inventory values**
- **Historical credit losses from dealer defaults have been minimal**
- **The Rating agencies' primary concern has been the health of the vehicle manufacturer and the impact a bankruptcy could have on dealer default rates and vehicle inventory values**
- **Credit enhancements in our floorplan securitization program are:**
  - **Cash reserve**
  - **Subordination of junior notes**
  - **Overcollateralization (available subordinated amounts)**
  - **Excess spread**

## ***FORD CREDIT FLOORPLAN STRUCTURE***

- **Certain adverse events called “Amortization events” cause principal to be paid to investors as the floorplan loans are collected, providing additional investor protection**
- **In a master trust, pool cash flow is allocated among all the outstanding series of securities**
- **The master trust has a sharing mechanism in which any cash flow allocated to a series but not needed by that series is reallocated to any other series that may need it, prior to release to Ford Credit**