

MEMORANDUM

TO: File No. S7-14-11

FROM: Arthur Sandel
Special Counsel
Office of Structured Finance
Division of Corporation Finance
U.S. Securities and Exchange Commission

RE: Conference call with SFIG representatives

DATE: January 29, 2014

On January 17, 2014, Arthur Sandel, David Beaning and Lulu Cheng of the Division of Corporation Finance and Sean Wilkoff and Igor Kozhanov of the Division of Economic and Risk Analysis participated in a conference call with the following representatives of the Structured Finance Industry Group, Inc. ("SFIG"): Sairah Burki of SFIG; Stuart Litwin of Mayer Brown LLP; Matthew St. Charles and Ryan Farris of Ally Financial Inc.; Sam Smith of Ford Motor Company; Phoebe Moreo of Deloitte & Touche LLP; and Ken Morrison of Kirkland & Ellis LLP.

The following staff of other federal regulators also participated: James Basham of the OCC; Kathy Russo, Phil Sloan, Gene Pocase, Steve Lake, William Haston, Robert Hendricks, Jacob Doyle, Suzanne Clair and Tom Lyons of the FDIC; April Snyder and Donald Gabbai of the Federal Reserve Board; Steve Schoen of the Federal Reserve Bank of New York; and Ankur Datta of the Department of the Treasury.

The participants discussed topics related to the Commission's August 28, 2013 joint proposed rules regarding credit risk retention. Handouts are attached to this memo.

Attachments



Risk Retention Re-Proposal

Follow up from 12/6/13 Auto Meeting

January 17, 2014

Agenda

- Representative Sample
- Eligible Horizontal Residual Interest (EHRI)
 - Revolving Transactions – Self Adjusting Approach
 - Simplified Approach for Simplified Structures
 - Relief for Truly Private Transactions
- We'd also be happy to further discuss Limitations on EHRI Distributions and the related Ford spreadsheet if desired by the regulators

Representative Sample

- In our meeting, the joint regulators appeared open to permitting the representative sample method if provided with assurance that it would be “representative” rather than merely “random”
- Construction of Representative Sample
 - Select a “Designated Pool” equal to 105.264% of unpaid principal balance of targeted securitized pool
 - Create the “Representative Pool”
 - Using a sampling method, select receivables totaling 5% of the unpaid principal balance from the Designated Pool
 - Validate the representativeness of the Representative Pool within a 95% confidence interval by measuring the following attributes:
 - Average Principal Balance
 - Weighted Average Remaining Term
 - Top 5 geographic percentages
 - We’d also be happy to include credit scores if consistent with the regulators’ goals

Representative Sample

- Prospectus (or Offering Memo) Disclosure:
 - Description of the policies and procedures used by the sponsor to:
 - Construct the Representative Pool
 - Test the representativeness of the Representativeness of the Representative Pool
 - Maintain isolation of Representative Pool during the period required under the Rules
 - Stratifications of Designated Pool and Representative Pool including:
 - Principal Balance
 - Remaining Term
 - Top 5 geographic percentages
 - We'd also be happy to include credit scores if consistent with the regulators' goals
- Servicing Standards: Servicers would be required to use the same collection and enforcement standards for both the Representative Pool and the Securitized Pool

EHRI - Revolving Transactions

- In our meeting, regulators requested information about revolving transactions that are not master trusts
- Two kinds of revolving auto loan/lease ABS transactions:
 - Revolving term transactions (example: Capital Auto Receivables Asset Trust 2013-4)
 - <http://www.sec.gov/Archives/edgar/data/893958/000119312513452816/d630108d424b5.htm>
 - Future additions of assets after initial closing date
 - Warehouse facilities provided by banks and ABCP conduits (see, for example, Exhibits 10.5 through 10.7 to the GM Financial Form 10-K)
 - <http://www.sec.gov/Archives/edgar/data/804269/000080426913000010/acf12311210-k.htm#sEBA1B1E5E6D11227DA15B72364B3FE86>
 - Future additions of assets after initial closing date
 - Future additional fundings after initial closing date
 - Commitments typically get renewed, so you don't know when amortization will begin
- These structures are used extensively by auto finance companies and are an important component of liquidity for them
- Problem: Difficult to project future cash flows/fair value without knowing the assets/funding/amortization in the future

EHRI - Revolving Transactions

- Proposed “Self Adjusting” Approach to EHRI:
 - Test fair value (or simplified approach) at each time additional assets are added (or incremental amounts are invested)
 - Testing to be done as if no future assets are added and that the deal amortizes thereafter
 - Intended to mirror what really happens in revolving transactions

EHRI - Simplified Approach

- Very important to our members to have an alternative that would be simpler
 - Consider a simpler alternative with greater than 5% retention (perhaps 6%)
 - Alternative could be permissible only with simpler structures
- Possible conditions were listed in our letter:
 - ABS principal amount sold to third parties $< 95\%$ of securitized pool balance
 - Asset WAC (or discount rate) $>$ ABS WAC
 - ABS are just traditional interest bearing securities (i.e., no I/Os)
 - Residual interest is a traditional equity interest

EHRI –Relief for Truly Private Transactions

- These transactions fall into two categories
 - Term transactions between small issuers and a single investor such as an insurance company negotiating their own note purchase agreement
 - Bank or ABCP-funded transactions often involving a single bank
- In these private transactions, typically there is:
 - No offering memo
 - Due diligence conducted by the investor
- Some of these transactions are structured as securitizations rather than typical bank loans
 - Issuer can get a lower cost of funds due to bankruptcy-remoteness
 - Investor has a safer investment due to bankruptcy-remote structure
- The Simplified Approach would be particularly useful in these situations
- Alternatively, we'd like to request an exemption for transactions offered under the following conditions:
 - Offering under Section 4(2) of the Securities Act of 1933
 - Investor is a QIB
 - No offering memo
 - Investor has the opportunity to perform due diligence
- Without relief, likely alternative is that these transactions would not be structured as securitizations

EHRI – Limitations on EHRI Distributions

- Apples vs oranges
 - Comparison of all cash flows with just principal repayment
 - Fair value/discounted dollars (CDPCFR) vs nominal dollars (CDPPRR)
- Problematic for many established structures, including:
 - Simple, proven, plain vanilla auto ABS structures that maintain substantially more than 5% risk retention over their lives
- As an alternative, we suggest a direct measure to achieve the same objective (as illustrated in the attachment):
 - *On the closing date, the projected fair value of the amount retained as of each payment date will not be less than the required 5% risk retention amount*

Assumptions		
Note coupon	1.297%	per annum
Servicing fee	1%	per annum
Average receivable yield	5.57%	per annum, incl. yield supp.
Excess spread	3.27%	per annum
Prepayment speed	1.4	ABS
Hard credit enhancement	10%	
Cumulative loss	1.25%	of initial gross receivable, through year 4
Discount rate for residual interest	10%	per annum
Discount rate per month	0.82%	
First interest period	37	days

	Month End Gross Receivable	Yield Supplement O/C	Month End Adjusted Pool Balance	Month End ABS Note Balance	Receivable Principal Collections (gross, no loss)	Receivable Interest Collections	Receivable losses	Receivable Principal Collections (net of losses)	Servicing Fee	Note Interest Payment	Note Principal Payment	Residual Cash Flow	Present Value of Cumulative Residual Interest at Payment Date	Total ABS Interest	Risk Retention Ratio	Present Value of Residual Interest at Closing Date	Present Value of Cumulative Residual Interest at Closing Date through Payment Date	Projected Cash Flow Rate	Principal Payment of All ABS Interest	Projected Principal Payment Rate
0	333,999,033	5,579,344	328,419,689	295,577,720									41,364,290	336,942,011	12%					
1	323,186,256	5,376,832	317,809,424	286,028,482	10,812,777	1,230,823	86,840	10,725,938	278,333	394,013	9,549,239	1,775,170	39,966,847	325,995,329	12%	1,721,123	1,721,123	4.2%	11,270,362	3.3%
2	312,534,506	5,178,634	307,355,872	276,620,285	10,651,749	1,192,438	86,840	10,564,910	269,322	309,149	9,408,196	1,770,680	38,522,490	315,142,775	12%	1,742,116	3,463,239	8.4%	22,420,675	6.7%
3	302,044,619	4,984,764	297,059,854	267,353,869	10,489,887	1,154,578	86,840	10,403,048	260,445	298,980	9,266,416	1,731,784	37,105,237	304,459,106	12%	1,690,048	5,153,287	12.5%	33,377,138	9.9%
4	291,717,432	4,795,126	286,922,306	258,230,075	10,327,187	1,117,246	86,840	10,240,347	251,704	288,965	9,123,793	1,693,131	35,715,064	293,945,140	12%	1,638,945	6,792,232	16.4%	44,139,877	13.1%
5	281,553,791	4,609,609	276,944,182	249,249,764	10,163,641	1,080,448	86,840	10,076,802	243,098	279,104	8,980,312	1,654,736	34,351,936	283,601,700	12%	1,588,806	8,381,039	20.3%	54,708,995	16.2%
6	271,554,545	4,428,083	267,126,462	240,413,816	9,999,246	1,044,186	86,840	9,912,406	234,628	269,397	8,835,948	1,616,619	33,015,796	273,429,612	12%	1,539,637	9,920,675	24.0%	65,084,580	19.3%
7	261,720,549	4,250,528	257,470,021	231,723,019	9,833,996	1,008,464	86,840	9,747,156	226,295	259,847	8,690,798	1,578,680	31,706,685	263,429,703	12%	1,491,328	11,412,004	27.6%	75,266,705	22.3%
8	252,052,664	4,076,927	247,975,738	223,178,164	9,667,885	973,287	86,840	9,581,045	218,100	250,454	8,544,855	1,540,923	30,424,642	253,602,806	12%	1,443,872	12,855,875	31.1%	85,255,432	25.3%
9	242,551,757	3,907,267	238,644,489	214,780,040	9,500,908	938,658	86,840	9,414,068	210,044	241,218	8,398,124	1,503,341	29,169,714	243,949,754	12%	1,397,248	14,253,123	34.5%	95,050,803	28.2%
10	233,218,697	3,741,543	229,477,154	206,529,439	9,333,059	904,582	86,840	9,246,219	202,126	232,141	8,250,602	1,465,932	27,941,948	234,471,386	12%	1,351,445	15,604,568	37.7%	104,652,850	31.1%
11	224,054,364	3,579,714	220,474,650	198,427,185	9,164,333	871,063	86,840	9,077,494	194,349	223,224	8,102,253	1,428,730	26,741,359	225,168,544	12%	1,306,481	16,911,049	40.9%	114,061,584	33.9%
12	215,059,639	3,421,768	211,637,872	190,474,084	8,994,725	838,104	86,840	8,907,885	186,712	214,467	7,953,101	1,391,709	25,567,989	216,042,073	12%	1,262,321	18,173,371	43.9%	123,277,007	36.6%
13	206,235,411	3,267,680	202,967,731	182,670,958	8,824,228	805,710	86,840	8,737,388	179,216	205,871	7,803,126	1,354,885	24,421,863	207,092,821	12%	1,218,968	19,392,338	46.9%	132,299,101	39.3%
14	197,582,573	3,117,439	194,465,134	175,018,621	8,652,838	773,884	86,840	8,565,998	171,863	197,437	7,652,337	1,318,245	23,303,019	198,321,640	12%	1,176,398	20,568,737	49.7%	141,127,836	41.9%
15	189,102,026	2,971,025	186,131,001	167,517,901	8,480,547	742,632	86,840	8,393,708	164,652	189,166	7,500,720	1,281,801	22,211,483	189,729,384	12%	1,134,612	21,703,349	52.5%	149,763,168	44.4%
16	180,794,674	2,828,428	177,966,247	160,169,622	8,307,352	711,956	86,840	8,220,512	157,585	181,059	7,348,279	1,245,545	21,147,291	181,316,913	12%	1,093,591	22,796,939	55.1%	158,205,038	47.0%
17	172,661,429	2,689,630	169,971,800	152,974,620	8,133,245	681,862	86,840	8,046,405	150,662	173,117	7,195,002	1,209,487	20,110,469	173,085,089	12%	1,053,331	23,850,270	57.7%	166,453,371	49.4%
18	164,703,208	2,554,615	162,148,593	145,933,734	7,958,222	652,354	86,840	7,871,382	143,885	165,340	7,040,886	1,173,625	19,101,024	165,034,776	12%	1,013,822	24,864,092	60.1%	174,508,078	51.8%
19	156,920,933	2,423,384	154,497,548	139,047,793	7,782,275	623,436	86,840	7,695,436	137,253	157,730	6,885,941	1,137,948	18,119,051	157,166,845	12%	975,041	25,839,133	62.5%	182,369,600	54.1%
20	149,365,909	2,295,944	147,069,965	132,362,969	7,555,024	595,111	86,840	7,468,184	130,767	150,287	6,684,825	1,097,416	17,169,155	149,532,544	11%	932,696	26,771,829	64.7%	189,986,581	56.4%
21	141,985,808	2,172,296	139,813,512	125,832,161	7,380,101	567,427	86,840	7,293,261	124,472	143,062	6,530,808	1,062,346	16,247,415	142,079,576	11%	895,578	27,667,408	66.9%	197,412,967	58.6%
22	134,781,566	2,052,440	132,729,127	119,456,217	7,204,241	540,343	86,840	7,117,402	118,322	136,004	6,375,947	1,027,473	15,352,600	134,808,814	11%	859,164	28,526,572	69.0%	204,648,078	50.7%
23	127,816,739	1,936,332	125,880,407	113,292,366	6,964,827	513,864	86,840	6,877,988	112,318	129,112	6,163,848	986,573	14,491,379	127,783,745	11%	818,283	29,344,855	70.9%	211,630,209	52.8%
24	121,026,431	1,823,962	119,202,469	107,282,222	6,790,308	488,305	86,840	6,703,468	106,514	122,450	6,010,144	952,665	13,657,034	120,939,255	11%	783,760	30,128,615	72.8%	218,424,113	54.8%
25	114,411,572	1,715,299	112,696,273	101,426,646	6,614,859	463,344	86,840	6,528,019	100,855	115,954	5,855,576	918,978	12,849,563	114,276,209	11%	749,923	30,878,538	74.7%	225,029,612	56.8%
26	107,973,098	1,610,344	106,362,754	95,726,478	6,438,474	438,986	86,840	6,351,635	95,343	109,625	5,700,167	885,485	12,068,993	107,795,471	11%	716,739	31,595,276	76.4%	231,446,518	58.7%
27	101,711,950	1,509,091	100,202,859	90,182,573	6,261,148	415,233	86,840	6,174,308	89,978	103,646	5,543,905	852,194	11,315,340	101,497,913	11%	684,206	32,279,482	78.0%	237,674,629	70.5%
28	95,629,077	1,411,545	94,217,532	84,795,778	6,082,873	392,092	86,840	5,996,033	84,760	97,472	5,386,795	819,098	10,588,630	95,384,408	11%	652,308	32,931,790	79.6%	243,713,732	72.3%
29	89,785,419	1,317,700	88,467,719	79,620,947	5,843,658	369,566	86,840	5,756,818	79,691	91,650	5,174,831	780,212	9,894,873	89,515,820	11%	616,308	33,549,097	81.1%	249,504,871	74.0%
30	84,151,108	1,227,533	82,923,575	74,631,218	5,634,310	347,950	86,840	5,547,471	74,821	86,057	4,989,729	744,813	9,230,850	83,862,067	11%	583,581	34,131,678	82.5%	255,078,181	75.7%
31	78,693,088	1,141,012	77,552,077	69,796,869	5,458,020	326,983	86,840	5,371,181	70,126	80,664	4,834,349	713,025	8,593,193	78,390,062	11%	554,149	34,685,827	83.9%	260,466,679	77.3%
32	73,412,304	1,058,119	72,354,185	65,118,766	5,280,794	306,628	86,840	5,193,944	65,578	75,439	4,678,102	681,454	7,981,901	73,100,668	11%	525,323	35,211,151	85.1%	265,670,105	78.8%
33	68,473,221	978,829	67,494,392	60,744,953	4,939,083	286,890	86,840	4,852,243	61,177	70,383	4,523,843	633,760	7,413,312	68,158,265	11%	484,600	35,695,751	86.3%	270,538,519	80.3%
34	63,724,162	903,104	62,821,058	56,538,952	4,749,060	268,523	86,840	4,662,220	57,061	65,655	4,206,001	602,026	6,871,815	63,410,767	11%	456,607	36,152,358	87.4%	275,191,127	81.7%
35	59,244,412	830,896	58,413,516	52,572,164	4,479,749	250,769	86,840	4,392,910	53,103	61,109	3,966,788	562,678	6,365,244	58,937,408	11%	423,307	36,575,666	88.4%	279,581,221	83.0%
36	54,928,640	762,164	54,166,477	48,749,829	4,315,772	233,913	86,840	4,228,932	49,370	56,822	3,822,336	534,138	5,882,897	54,632,726	11%	398,716	36,974,382	89.4%	283,802,273	84.2%
37	50,777,722	696,853	50,080,869	45,072,782	4,150,919	217,627	86,840	4,064,079	45,774	52,620	3,677,047	506,195	5,424,736	50,497,518	11%	374,671	37,37,			