FitchRatings

One State Street Plaza
New York, NY 10004

T 212 908 0500 / 800 75 FITCH
www.fitchratings.com

November 15, 2010

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

*Re:* *Proposed Rule relating to Issuer Review of Assets in Offerings of Asset-Backed Securities, Release Nos. 33-9150 and 34-63091; File Number S7-26-10*

Ladies and Gentlemen:

Fitch, Inc. ("Fitch") submits this letter in response to the request of the Securities and Exchange Commission (the "Commission") for comments on the proposed rule relating to Issuer Review of Assets in Offerings of Asset-Backed Securities (the "Proposed Rule"). The various components of the Proposed Rule would require a review of assets underlying ABS offerings to be performed, and disclosure of the results of such review. Fitch sets forth below comments relating to those items in the Proposed Rules that are of concern to us.

Review of assets

Investors and others are increasingly requiring third party verification of the information provided about the assets underlying asset-backed securities offerings. In addition, Section 932(a)(8) and Section 933(b)(2)[1] of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act") specifically reference third party verification of information provided by the issuer.

Since the provisions of Section 933(b)(2) referenced in footnote 1 refer to a reasonable verification from sources "independent (emphasis added) of the issuer and underwriter[,]" the clear inference of the provisions of the Dodd-Frank Act is that the verification of information provided by issuers was intended to be subject to third party verification. Since rating agencies do not have the resources to be able to conduct reasonable verification for all asset classes which

[1] "(ii) to obtain reasonable verification of such factual elements (which verification may be based on a sampling that does not amount to an audit) from other sources that the credit rating agency considered to be competent and that were independent of the issuer and underwriter."

they rate, they will necessarily have to rely on independent third parties to conduct a reasonable verification of the factual elements relied upon in conducting it rating analysis. Rule 193 as currently proposed requires an issuer to conduct a review of assets, but an issuer review of assets would not satisfy the requirement to obtain a reasonable verification of assets from other sources independent of the issuer and underwriter. We believe, therefore, that rather than requiring issuers to perform the reviews, issuers should be required to retain independent third parties to provide verification of the assets underlying ABS transactions and that the results of such reviews must be disclosed to investors and rating agencies in accordance with the provisions of the Dodd-Frank Act.

This requirement would be consistent with, and facilitate the provisions of, Section 15(E)(s)(4)(B)-(D), which requires third party due diligence providers to provide a certification to an NRSRO that it has conducted its review in such a manner as to allow the NRSRO to provide an "accurate" rating, and requiring the NRSRO to disclose such certification in connection with its rating. Fundamentally, we agree that all investors benefit from increased transparency, which is enhanced when asset reviews are conducted and disclosed for both public and private offerings, whether or not the transactions are rated by an NRSRO, and whether or not such transactions are targeted primarily to US investors. Verification of assets is most reliable and useful to investors when such verification is performed by a competent, independent third party, which is why we presume the Dodd-Frank Act refers to verification from parties other than the issuer and underwriter, and to disclose the contents of such verification. Any other construction of the Dodd-Frank Act seems wholly inappropriate.

Nature of Asset Review

As proposed, Rule 193 would not specify the type or level of review an issuer is required to perform. The Commission has asked whether disclosure, without mandating the nature of review to be conducted, is sufficient, or whether the Commission should mandate a minimum level of review that must be performed on asset pools.

Fitch believes that the SEC should mandate the minimum level of review that must be performed on asset pools. Without such mandate, we do not have confidence that all issuers would undertake a meaningful review of the assets, in light of the cost considerations that such review would entail. Our view is informed by the challenges we are currently encountering in our attempts to obtain independent third party verification reports. We are mindful, however, that the objective of having an appropriate review of the assets be properly balanced with other considerations such that securitizations do not become cost prohibitive.

Given the wide variety of assets that are securitized, the nature of the asset review will necessarily vary depending on the asset. We agree that it would be appropriate for sampling methods to be used for asset pools consisting of large groups of loans (RMBS, credit cards, auto loans and leases, equipment leases, student loans, etc.). In order to ensure consistency, parameters should be set out to determine whether sampling is appropriate for each asset class. For sampling methods to be most useful, sampling should be conducted in a manner appropriate to provide confidence that a representative portion of the pool has been examined. A common standard that is used regularly in the accounting industry, for example, requires a sample size be computed using a 95% confidence level and a 5% confidence interval. To the extent any issues are surfaced from the initial sampling, further review should be conducted.

With regards to pools such as CMBS where the assets are much more limited in number, but large in dollar value, a review of a majority of the assets in the pool should be undertaken, as is Fitch's current practice with regards to CMBS assets. Lastly, for pools of revolving assets such as in master trusts, we believe that issuers should provide updated disclosure of independent, third party reviews of the accounts or assets added to the pool after the offering transaction has concluded, for periods as are appropriate for the relevant asset class.

We attach hereto as Appendix A the key rating factors and performance data (where applicable), which Fitch considers in connection with each ABS asset class currently rated by Fitch. This information may be helpful to the Commission in considering the minimum level of asset review that should be conducted in connection with different asset classes, as well as in the Commission's consideration of the format and content of the written certification which third party due diligence providers are required to provide rating agencies pursuant to Section 15E(s)(4)(B) of the Dodd-Frank Act. In any review to be performed for an ABS securitization rated by Fitch, it is critical that, at a minimum, each of these factors be verified. We believe that any error in this information could result in an inappropriate investment decision being made by investors in the securities. As Fitch reaches its ratings determination based on an analysis of loan level or pool level information it receives from the sponsor, data should be verified against the information provided to Fitch. We would recommend that the Commission require that issuers represent that the information they have provided to the rating agencies is consistent with that provided in the offering document.

Independent Third Party Due Diligence Providers

We attach as Appendix B hereto Fitch's report published on December 2, 2008, titled "US Residential Mortgage Third Party Loan-Level Review Criteria." This report describes Fitch's expectations as to the points addressed in third party loan level reviews for RMBS transactions, which may be helpful to the Commission in considering the requirements for third party reviews for other asset classes. As described in the report, Fitch expects a review company to be an independent company with no ties to the loan originator, the issuer of the notes, or the security underwriter, that it would need to have appropriate company and management experience for the type of loans being reviewed and have the procedures and controls, staff experience levels, technology and tools to adequately conduct its review.

Fitch acknowledges there may not exist at this time third parties (other than accountants) established to conduct reviews for all asset classes. With the increased demand for such services, however, we expect the market to address this need going forward. To the extent that the Commission proposes to impose expert liability on such third party due diligence providers, however, we are concerned that this action may have a chilling effect on the desire of parties to enter the field and provide this service, as liability considerations may be prohibitive. If the Commission does not mandate that all reviews be conducted by independent third parties, therefore, we would expect that issuers would conduct the reviews themselves, and very rarely use such third party verifiers. We would suggest that it might be more productive for the Commission to consider alternative methods of addressing the concern of maintaining the quality of third party reviews, such as the creation of appropriate industry standards (e.g., independence, rigorous methodologies, transparency) and oversight.

Disclosure Regarding Exception Loans

Fitch reiterates its position that greater transparency of information is beneficial to investors, and supports the Commission's proposal in Item 1111(a)(8) of Regulation AB to require that issuers disclose how the assets in a pool deviate from the disclosed underwriting criteria, as well as data on the amount and characteristics of those assets that did not meet the disclosed standards. It would be very useful to know which entity (sponsor, originator or underwriter) determined that such assets should be included in the pool even though underwriting standards were not satisfied, and the factors used to make such determination.

Filing of Form ABS-15G

Lastly, Fitch supports the proposal to require Form ABS-15G to be filed within 5 business days prior to an initial offering of ABS securities to investors since Fitch believes that the Commission should provide sufficient time for investors to review the findings and conclusions contained therein.

Thank you for giving us the opportunity to provide our comments. We hope you find them useful, and that you will give them due consideration. Please call me at (212) 908-0630 with any questions that you might have concerning our comments or if you wish to discuss this matter further at your convenience.

Very Truly Yours,

Kevin Duignan
Group Managing Director
US Structured Finance

# SEC Proposed Rules for Data Verification

*US Asset Backed Securities, CMBS, RMBS, Structured Credit*

## Student Loans- Federal Family Education Loan Program ("FFELP")

**Key Rating Factors**

- Loan type (i.e. Stafford, PLUS, or consolidation)
- School type (four-year, two-year, proprietary, or unknown)
- Loan status (in-school, grace, deferment, forbearance, or repayment)
- Weighted average loan age
- Loan interest rate
- Special Allowance Payments (SAP) Margin
- Servicer Fees
- Administration Fees
- Servicer net claims reject rate
- Remaining Term
- Principal balance range
- Days delinquent
- Reinsurance
- Floor income eligibility
- Date of disbursement
- Student domicile (State)
- Guarantor
- School
- Borrower benefits

## Private Credit Student Loans

**Performance Data**

- Historical cumulative defaults by repayment cohort
- Historical cumulative recoveries by default cohort

**Key Rating Factors**

- Cosigned vs. non cosigned
- Fair Isaac Corp. (FICO) score or equivalent risk segmentation scheme
- School type (four-year, two-year, proprietary, or unknown)
- Marketing channel (school certified vs. direct-to-consumer)
- Grade level (freshmen, sophomore, etc.)
- Seasoning
- Borrower Benefits

## Credit Card ABS

**Performance Data**

- Gross principal losses by vintage by reason (contractual, bankruptcy, fraud)
- Monthly Payment Rates (MPRs)
- Gross Yield and components (interest, fees, interchange), cash collected
- Delinquency Roll Rates

**Key Rating Factors**

- FICO score or equivalent credit risk assessment

- Geographic concentration (by state)
- Seasoning (account age)
- Annual percentage rates (APRs).
- Credit limit
- Product and segment mix (e.g. rewards, small business, retailer)
- Dilution (to evaluate seller's interest)

## *Auto Loan ABS*

**Performance Data**

- Historical portfolio/securitization pool factors
- Historical Vintage Loss Portfolio Performance
- Historical portfolio/securitization recovery rate and recovery lag data
- Historical portfolio/securitization prepayment rate data
- Historical securitization performance (gross/net losses)
- Managed portfolio delinquency and default/loss data (by buckets

**Key Rating Factors**

- Vehicle Make / Model / new-used / segment / vintage
- Loan Term (original/remaining)
- Loan balance (original/remaining)
- Seasoning
- FICO Score / or equivalent credit tier or score
- State
- Internal Credit Scores (tiers)
- APRs (all and subvented/nonsubvented)
- Days delinquent (times 30 day delinquent)
- Loan to value ratio (LTV)
- Replines (for modeling purposes)

## *Dealer Floorplan ABS*

**Performance Data**

- % of sold out of trust (SOT) of total defaults
- Monthly data (9 months prior to peak default and 3 months after unusual spikes in charge-offs):
  i. Number of defaulted dealers
  ii. Dealer grades for defaulted dealers
  iii. Defaulted Dealer Credit Lines/Utilization
  iv. Defaulted Inventory (units/dollars)
  v. Default Reason-How was it determined? Missed curtailment payment vs. inspection SOT
  vi. Recoveries: broken out by inventory disposal proceeds and other recoveries
  vii. Total # of dealers at the time of default
- Dealer grades for the total dealer population
- Total inventory outstanding (units/dollars)

**Key Rating Factors**

*Loan Financing Terms*

- Credit line size and utilization rate

- Financing rates/Asset Yield
- Curtailment Terms
- Repayment Terms (in months) by product-line

*Securitized portfolio Experience:*

- Aging Experience (in 30 day buckets to at least 360+)
- Monthly Payment Rate
- Monthly Data: Gross Losses, Recoveries, Delinquencies
- Yield - with breakdown of Libor/Prime/Fixed with spreads
- New Sales Rate
- Concentration Limits (specified in securitization program) and actual historical experience:
- State Concentrations
- Dilutions

## *Auto Lease ABS*

**Performance Data**

- Historical recovery rate and recovery lag data
- Historical prepayment rate data
- Historical Residual Loss Data (over time), stratified by
- Make / Model / Vehicle Segment
- Lease Term
- Managed portfolio delinquency and default/loss data (Currently tied out for the OM)

**Key Rating Factors**

- Vehicle Make / Model / Year
- Lease Maturity Month
- Weighted average coupon, weighted average original and remaining term
- FICO Score / Credit tier or score
- Securitization Values
- Base Residual Value
- Lease Rate
- Lessee State

## *Equipment ABS*

**Performance Data**

- Historical portfolio/securitization pool factors
- Historical portfolio/securitization recovery rate and recovery lag data
- Historical portfolio/securitization prepayment rate data
- Historical securitization performance (gross/net losses)
- Historical Managed/Securitization Residual Realization Data

**Key Rating Factors**

- Summary of Top 20 Obligors over the life of the transaction
- Equipment type
- Business unit
- Loan type
- # of Loans
- Loan Term (original/remaining)

- Loan balance (original/remaining)
- Seasoning
- Geographic concentrations
- APRs
- Days Delinquent (times 30 day delinquent)
- Replines (for modeling purposes)

## *Timeshare ABS*

**Performance Data**

- Historical portfolio/securitization pool factors
- Historical portfolio/securitization recovery rate and recovery lag data
- Historical portfolio/securitization prepayment rate data
- Historical securitization performance (gross/net losses)
- Historical Managed/Securitization Residual Realization Data

**Key Rating Factors**

- Business unit/brand
- Loan type
- # of Loans
- Loan Term (original/remaining)
- Loan balance (original/remaining)
- Seasoning
- Geographic concentrations
- Interest Rate
- Days Delinquent (times 30 day delinquent)
- FICO scores (Original/Current)
- WA Equity
- Foreign Obligors
- Replines (for modeling purposes)

## *Aircraft Lease ABS*

**Performance Data**

*Historical data on the leasing activities, including:*

- Lease Rates / Lease Rate Factors
- Reposession Downtime and Costs
- Remarketing Downtime and Costs
- Lease Renewal Data
- Default Rates and Detail on Historical Default Experience
- Maintenance Expenses
- Historical Asset Depreciation Experience
- Histrorial Asset Disposition Experience

**Key Rating Factors**

- Aircraft / Engine types and variants
- Supported airframes (for engines)
- Geographical location (lessee and registration)
- Appraisals and full appraisal information

- Purchase price relative to current appraisal
- Last scheduled delivery date for the aircraft (or supported aircraft for engines)
- Manufacture date / Current age
- Lessee and credit rating (If applicable)
- Original term
- Remaining Term
- Lease rate (and details on computation if there is a floating component)
- Lease begin date
- Lease end date
- Security deposit or LOC, if applicable and description:
- Return conditions

## *CMBS*

**Key Rating Factors**

- Property Location (Street Address, City, State, Zip Code, County)
- Occupancy (%) and date
- Property Type
- Property Sub-Type
- Largest Tenant #1
- Cut off date loan balance (allocated by property)
- Pari Pasu (Y/N)
- Whole A note balance
- Appraised Value
- Balloon Balance
- UW Net Cash Flow
- Monthly Debt Service
- UW DSCR
- Interest Rate, Fixed/Floating Loans
- Ceiling Rate
- Maturity Date
- ARD date
- Original Loan Term
- Remaining Loan Term
- Amortization Type
- Lien Type
- Earnouts (Y/N)
- Deferred maintenance amount
- Environmental issues
- Recourse (Y/N) and Recourse Carveouts (Y/N)
- Reserves (Taxes, Insurance, Capital Expenditures, TI/LC)

## *RMBS*

**Key Rating Factors**

**Loan Attributes and Terms**

- Loan and amortization type (i.e. fixed rate or ARM type)
    - ARM data:

        - ARM Index
        - ARM look-back days
        - ARM rounding flag
        - ARM rounding factor
        - Current coupon
        - Initial coupon
        - Gross margin
        - Lifetime rate floor
        - Initial rate cap
        - Periodic rate cap
        - Lifetime rate cap
        - Months to first reset
        - Months between subsequent resets
        - Fully indexed rate
    - Additional HELOC data:
        - Maximum 12-month draw amount
        - HELOC amortization method
        - Revolving term
- Lien status
- Mortgage loan note date
- First payment date
- Maturity date
- Last paid date
- Loan purpose
    - If cash-out, cash-out amount
- Original loan amount
- Current loan amount
- Original amortization term
- Original term to maturity
- Remaining term to maturity
- Original Interest Only term
- Current senior lien(s) amount
- Current subordinate loan(s) amount
- Original LTV
- Original Combined LTV
- Borrower-paid MI coverage
- Borrower-paid MI company
- Lender-paid MI coverage
- Lender-paid MI company
- Lender-paid MI fee
- Negative Amortization limit percent
- Buydown period or employee subsidy period
- Prepayment terms
- Interest payment type

**Additional Borrower Credit Items**

- Total number of borrowers

- Self employed flag
- Borrower FICO/Vantage scores
- FICO model used
- Scheduled P&I payment
- Borrower Income
    - Borrower income verification level
    - Borrower employment verification level
- Borrower Asset verification level
- Borrower Reserves
    - Liquid/Cash reserves
    - Total monthly debt
- Current 'other' monthly payments
- Mortgage payment history
- 'Other' Payment history
- Bankruptcy history
    - Bankruptcy type
    - Bankruptcy petition date
    - Bankruptcy resolution date
- Modification effective payment date
    - Effective payment date
    - Total Capitalized amount
    - Updated DTI – front-end
    - Updated DTI – back-end
    - Total deferred amount
    - Pre-mod interest (note) rate
    - Pre-mod P&I payment

**Property**

- Property postal ('zip') code
- Property State
- Property City
- Property value
- Property type
- Occupancy
- Number of units
- Property valuation type
- Property valuation date

## *Structured Credit*

**Key Rating Factors**

- Obligor legal name and parent/subsidiary relationship, if relevant
- Public Entity Y/N
- Rating
- Debt Type/Asset Seniority
- Amortization Schedule, if contractual
- Unique Payment Features - PIK, Asset-Based
- Stated Maturity Date

- Interest Rate and Index
- Payment Frequency
- Standard Industrial Classification (SIC) Industry Code
- Country
- Notional Balance

Residential Mortgage
Criteria Report

# U.S. Residential Mortgage Third-Party Loan-Level Review Criteria

**Analysts**

Diane Pendley
+1 212 908-0777
diane.pendley@fitchratings.com

Roelof Slump
+1 212 908-0705
roelof.slump@fitchratings.com

**Related Research**

- *U.S. Residential Mortgage Originator Review Criteria, Dec. 2, 2008*
- *U.S. Residential Mortgage Loan Representations and Warranties Criteria, Dec. 2, 2008*

## Summary

One of the major causes of the poor performance in U.S. RMBS over the past two years has been the poor underwriting quality in practice at the loans' origination. Therefore, in conjunction with its recently revised originator review criteria, Fitch Ratings will require third-party loan-level reviews (reviews) on all residential mortgage pools that Fitch is asked to rate. The reviews will be conducted by a "due diligence" company (review company) prior to Fitch providing a rating on the transaction.

A review company will be an independent company with no ties to the loan originator, the issuer of the notes, or the security underwriter. It will need to have the appropriate company and management experience for the type of loans being reviewed and have the procedures and controls, staff experience levels, technology, and tools to adequately conduct and report on the reviews described in this report.

The review company will have its employees inspect the loan files and loan data tape and will provide Fitch with a report that details all instances where the review determines that a loan was originated and underwritten outside the stated guidelines of the originator's loan origination program. Additionally, the review is expected to detail any underwriting information that is missing or different to certain minimum standards outlined below.

## Review Criteria

The review company will indicate and describe in as full a detail as possible all loans that did not strictly meet in one or more respects:

- The stated originator guidelines.
- The applicable federal, state, or local laws and regulations.

Additionally, the review company will detail each loan that has missing or different underwriting standards. If a loan does not meet the requirements in the stated originator guidelines and the applicable federal, state, or local laws and regulations or if 10% or more of a loan's documents are missing or incomplete, that loan will be recorded as an underwriting exception. The report shall state the nature of each underwriting exception, as well as any compensating factors that, in the review company's opinion, would have warranted a deviation from the originator's guidelines. If 15% or more of the loan sample contains underwriting exception loans Fitch may, depending on the strength of the compensating factors, decide that it is not able to rate the transaction.

**RMBS Loan-Level Review Categories**

- Sample size
- Review methodology
- Loan files
- Data quality
- Originator guidelines

The report also should contain a certification by the review company to Fitch that all aspects of the review methodology described in this report were completed for each loan in the sample. In addition, there should be certification that there was sufficient time to complete the review and report, the reviewers had the appropriate levels of experience, and to the best of its knowledge, the review company and reviewers were not directly or indirectly improperly influenced in the scoring and outcome of the review.

### Sample Size

- For prime pools from established originators and loan programs, the randomly selected minimum sample size is to be the larger of 200 loans or 10% of the pool.
- For subprime/Alt-A and all other product types, the randomly selected minimum sample size is to be the larger of 400 loans or 20% of the pool.
- If originators or its loan programs have had less than two years of performance history, the sample size should be doubled.

### Review Methodology

The review should be performed by a review company employee who has at least three full years of experience as a mortgage underwriter in the product type being reviewed. The employee should have specific training in credit, value, compliance, and legal. If multiple reviewers are being used for different aspects of the review, specific training in the area for which the reviewer is responsible is acceptable.

In addition to the initial review, there should be a quality control review. The quality control review will consist of a randomly selected sample of a reviewer's files by another review company employee who has at least seven years' experience as a mortgage underwriter in the product type being reviewed. The number of files reviewed in the quality control review will depend on the experience of the reviewer and according to the following:

- Reviewer has three to five years' experience — 50% of the files.
- Reviewer has five to seven years' experience — 25% of the files.
- Reviewer has greater than seven years' experience — 10% of the files.

All loans that are found to be underwriting exceptions are to be documented. However, at least 10% of the loans that are underwriting exceptions must be re-underwritten by an employee having at least seven full years' underwriting experience.

### Loan Files

The reviewer should check the loan files being reviewed for the following:

- Confirm the presence or absence of relevant credit, property valuation, compliance, and legal documents, including documents such as loan application, income, employment and asset documentation, occupancy, credit report, property appraisal, and legal documents.
- Review the loan documentation for authenticity, consistency, and accurate calculations.
- Determine that the loan was originated in compliance with the originator's stated underwriting guidelines, noting any exceptions and/or compensating factors.
- Provide an opinion on whether the originator ascertained that: the borrower has the ability and willingness to repay the loan; the value is reasonably supported; federal, state, and local laws were adhered to, including an explanation of any preemption that applies; and the enforceability of the mortgage loan documents.
- Review the originator's property valuation and fraud safeguards, specifically with

respect to appraisals, income, and occupancy to confirm that the originator utilized a fraud tool and related output in accordance with the originator's stated guidelines, noting any exceptions. If no fraud tool was utilized by the originator, the reviewer will document and report on the results of the additional checks and/or verifications performed by the reviewer, including utilization of fraud tools, to identify potential misrepresentation or fraud.

- Examine the servicing file for loans with 90 days or more seasoning at the time of the review and report on any late payments or other delinquencies and on any evidence of fraud (including occupancy fraud).
- Confirm that the loan was originated in compliance with all enforceable federal, state, and local, predatory lending and high cost, and Truth in Lending Act (TILA) and Regulation Z laws and regulations. The reviewer is to state that there is no reason to believe the mortgage documents are not enforceable.

## Data Quality

The reviewer is to verify that all the Fitch data fields are on the tape and filled in. In addition, the reviewer should confirm that that the data on the tape matches and correctly represents the contents of the loan file under inspection. Any differences should be provided on a data exception report.

## Originator Guidelines

The reviewer is to confirm whether each sampled loan was within all stated underwriting guidelines of the originator.