March 22, 2010

BY ELECTRONIC MAIL

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

Re: SR–FINRA–2009–065
To Require the Reporting of Transactions in Asset-Backed Securities to TRACE

Dear Ms. Murphy:

The Association of Mortgage Investors (the "Association") is a new trade association made up of asset management firms who are active in the non-agency mortgage backed securities and other institutional mortgage products. These asset management firms invest billions of dollars on behalf of their clients, which include public and private sector pension funds, university endowments as well as individual investors.

The Association is pleased to submit this letter in response to the request for comments of the Securities and Exchange Commission ("SEC" or "Commission") on proposal by the Financial Industry Regulatory Authority, Inc. ("FINRA") to expand TRACE to include the reporting (but not public dissemination) of Asset-Backed Securities (SR–FINRA–2009–065, the "Proposal").

While, to date, the Association has not been actively involved in the issue of secondary market transparency generally or reporting asset-backed securities to TRACE specifically, we recently completed a White Paper entitled "Reforming the Asset-Backed Securities Market." I have attached a copy of this document as Exhibit I for your reference.

In our White Paper, we suggest several methods to aid in the restoration of the United States securitization market. We believe it is important for the government to consider the policy recommendations of investors, whose participation and capital are needed for there to be an asset-backed securities market at all. Our recommendations support healthy and efficient markets, with more information made more widely available to participants, regulators and observers; incentivize positive economic behavior among market participants; reduce information asymmetries that distort the spread between price and value and are entirely consistent with the government's traditional roles of standard-setting in emerging capital markets.

With respect to price transparency issues in the secondary mortgage market, our White Paper specifically proposes that:

> **Certain asset-backed securities could be simplified and standardized so as to encourage increased trading in the secondary market on venues, such as exchanges, where trading prices are more visible to investors and regulators.** This could result in better price discovery, additional market transparency, additional liquidity and reduced bid/ask spreads. In the interim, investors should be strongly encouraged to buy only those financial instruments which they have an understanding of and are able to analyze completely, including the instruments' current market value. All dealers should be required to disclose historical trade prices on these simplified and standardized asset-backed and structured finance securities daily.

The issue of transparency in the securitization is critical to rebuilding a private mortgage market in the United States. Ensuring optimal and deep liquidity in the secondary market is important to that effort. Generating appropriate price transparency in the secondary market for asset-backed securities is also an important element to the reformation of the U.S. asset-backed securities markets.

As an organization comprised of many of the prominent investors in these products, we would be pleased to be involved in discussions regarding price transparency and market structure generally with the Commission and/or its staff.

Sincerely,

Association of Mortgage Investors
c/o Micah S. Green, Esq.
Patton Boggs LLP
2550 M Street, NW
Washington, DC 20037

<u>Exhibit I</u>

White Paper: Reforming the Asset-Backed Securities Market

White Paper

Reforming the Asset-Backed Securities Market

Association of Mortgage Investors

March 2010

Introduction

In the two and a half years since the financial crisis began, it has become clear that the continued health of the securitization markets is crucial not just to U.S. economic recovery but to the financial system as a whole. There are three sources of residential and commercial mortgage capital in the United States – bank balance sheets, which are full and stressed; the securitization market, which is effectively shut down; and the government (Fannie Mae, Freddie Mac, FHA, etc.). For other types of debt capital, there are only two sources – banks and the securitization market – as the government does not directly provide capital the way it does for mortgages. Restoring the securitization market is necessary to get more private capital flowing to those who wish to use it, and accordingly to reduce the government's role of providing public capital to, and allocating that capital among, private borrowers.

The structures and mechanisms that have defined the securitization market to date have been constructed by issuers, underwriters, credit rating agencies and asset servicers with minimal disclosure-based, procedural or substantive regulation by Congress, financial regulators or the SEC. Investors provide the capital that make the securitization markets work yet have been ignored in market structure discussions. They have been told by other parties to securitization to "take it or leave it" on disclosures, definitions and structures, in other words - "just buy the securities we offer you". Now that poor credit underwriting, moral hazards, inadequate disclosures, asset servicer conflicts of interest, ratings agency failures, and logistical obstacles to working out bad collateral assets have scared investors away from the securitization markets, it is important for the government to consider the policy recommendations of investors, whose participation and capital are needed for there to be an asset-backed securities market at all. In fact, while issuers suggest otherwise and ideally it would be great if a consensus between issuers and investors could emerge, there need not be a consensus as investors ultimately provide the capital and have the responsibility to define the terms on which they will commit their capital.

We believe that the following recommendations support healthy and efficient markets, with more information made more widely available to participants, regulators and observers; incentivize positive economic behavior among market participants; reduce information asymmetries that distort the spread between price and value and are entirely consistent with the government's traditional roles of standard-setting in emerging capital markets.

1. **Provide loan-level information that investors, ratings agencies and regulators can use to evaluate collateral and its expected economic performance, both at pool underwriting and continuously over the life of a securitization.** Currently loan-level financial and related due diligence information is not required to be publicly disclosed. Issuers, underwriters and asset servicers already have this information and it costs little to make it publicly available on EDGAR or similar systems. Investors in asset-backed securities have both the interest and the ability to analyze such information to help them make better purchase and sale decisions relating to asset-backed securities.

Data should be provided on a daily, or at least monthly, basis in both the primary and secondary markets. To ensure adequate transparency, enhanced disclosure rules should be required both for deals with and without static pool data such as asset-backed commercial paper. Data on the specific underlying collateral in each pool should be made available for a reasonable period – not less than two weeks – before a deal is sold and brought to market. This should be done to enhance investor due diligence, to foster the development of independent analytical data providers, and to reduce reliance on rating agencies. To ensure the accuracy of the information, loan-level data offered by issuers, underwriters or assets servicers for investors should be accompanied by an auditor attestation verifying that the data has been properly aggregated, calculated and published. The loan-level data should be available in an electronically manageable and industry standardized format. After the deal is sold, all data fields in the pre-issuance disclosures and material information about the loan-level collateral in the pool should be updated and be similarly disclosed on a daily, or at least monthly, basis. The data already exists and the creation of standard data fields and automation of this process would create little regulatory burden.

Capital markets would be less volatile if investors could fully model the expected performance of underlying loan-level collateral before a deal comes to market and, on a regular basis, assess the deviance from expectations. The provision of loan-level performance to investors on a regular basis would allow any degradation of performance to be observable and therefore priced in over incremental periods. By requiring that investors receive early and regular disclosures of all available information about collateral performance, the importance of NRSROs' ratings will be diminished to the level of equity analysts' research notes.

The fact that investors have to pay to subscribe to services such as Loan Performance to get data on collateral underlying asset-backed securities they are offered and may already hold is outrageous in light of the no-cost extensive public disclosure required for corporate securities. Arguments that the amount of loan-level information exceeds the capacity of investors to process and analyze – when issuers, underwriters and asset servicers have no problem processing and analyzing the very same data – are absurd on their face.

2. **Require a "cooling off" period when asset-backed securities are offered so that investors have sufficient time to review and analyze loan-level information before making investment decisions.** Currently investors in primary offerings of asset-backed securities are forced to make decisions as to whether or not they want to purchase immediately after deals come to market. As with existing SEC requirements relating to new issues of equity and debt securities, issuers should have to wait for a reasonable period of time before closing offerings of asset-backed securities. A two-week period would permit investors to properly analyze loan-level collateral and independently determine whether projected performance expectations are adequate.

3. **Make deal documents for all asset-backed securities and structured finance securities publicly available to market participants and regulators.** This will substantially increase market liquidity for such securities after they are sold. In the lead-up to the financial crisis, even primary financial regulators could not analyze or even have access to deal documents of asset-backed and structured finance securities (e.g. CDOs) that their regulated institutions held. The common practice of making fundamental asset-backed and structured finance deal documents proprietary and subject to confidentiality obligations is fundamentally inconsistent with properly functioning capital markets and prudential regulation of financial institutions.

4. **Develop, for each asset class, standard pooling and servicing agreements with model representations and warranties as a non-waivable industry minimum legal standard.** Right now every pooling and servicing agreement for a securitization is custom-written. Representations and warranties vary tremendously from deal to deal, even within the same fundamental asset class (mortgages, credit cards, etc.). This requires investors to spend tremendous amounts of time analyzing the differences between different transactions' legal terms and subjectively weighing the economic meaning of those terms before coming to investment decisions – or alternatively to ignore these differences of legal terms in the interest of time, to the peril of investors when problems develop in the market.

This lack of standardization and the length of the legal documentation effectively created opacity in the securitization market, which substantially contributed to the recent problems experienced by market participants. When collateral pool performance deteriorated, panic set in and investors began to question the value of their securities, they knew that they did not have the time to read all of the different several-hundred-page deal agreements to evaluate their holdings. This reinforced the rush to liquidate positions. What investor wants to be the last one holding a security the terms of which he doesn't fully understand? Potential buyers of these securities in turn would not step into the market without having read the documents themselves, causing the entire fixed-income market worldwide to freeze up.

Standardizing legal documentation gives investors a common framework with which to evaluate their potential and actual holdings of asset-backed and structured finance securities based largely if not solely on collateral pool performance. The asset-backed securities market as a whole would thereby become more homogenous and therefore more liquid. Investors should be able to rely on certain baseline assurances as to the nature of the collateral underlying their securities. Having a single standard set of representations and warranties that must be met or exceeded in every transaction gives investors comfort about the assets in which they have an interest, and reduces the overhead costs of investing in these securities. In addition, standardized representations and warranties would streamline resolution of disputes as to whether representations and warranties are met by individual assets within collateral pools.

Model agreements for the asset-backed securities market should be drafted with the best interests of the investing public, and with clarity of rights and responsibilities, at their cores.

5. **Develop clear standard definitions for securitization markets.** Without a common language and agreement on the meanings of fundamental concepts – such as "delinquency" and "default" – the value of data is diminished, the ability to compare securities across different pools is diminished, and the concepts of relative collateral pool performance and economic value become seriously muddied. There are no such standard definitions currently, and as a result servicers with very similar underlying collateral pools and servicing standards can produce radically different reports of collateral performance. For example, the term "delinquency" can be determined either on a contractual or recency-of-payment basis. Even among firms that would define delinquency on the same basis, each servicing agreement can have different interpretations on reporting of delinquencies – some may report advances that a servicer makes to a pool that could be applied to reduce stated delinquencies, but other servicing agreements may not. When no one agrees on what delinquencies are and how they must be reported, then how do we know what the term "default" means? How can anyone really understand what is happening if there is so much variability deal-to-deal and there are no industry-standard

practices? This is a huge problem that interferes with investors' ability to make investment decisions among various deals and issuers. The lack of clear standard definitions reinforces the complexity from the lack of standard contracts in securitization deals, and also makes it harder for capital markets to function.

Conversely, if everyone is using common language in loan origination and securitization then it becomes very hard to game the system as issuers and servicers have.

6. **Directly address conflicts of interest of servicers that have economic interests adverse to those of investors, by imposing direct fiduciary duties to investors and/or mandatory separation of those economic interests, and standardize servicer accounting and reporting for restructuring, modification or work-out of collateral assets.** Servicers of mortgage or other financial asset pools often have economic interests that differ from those of investors. Simple contracts between servicers and securitization trustees, which themselves are subject to little or no accountability to investors, have not sufficiently aligned the interests of servicers to those of investors over time.

Where servicers are charged with enforcing representation and warranty claims on specific collateral pool assets so they are put back to originator affiliates of the servicers at par, the servicers have a conflict of interest and appear to have been delaying in carrying out such put-backs so as to avoid losses to their affiliates. Where servicers have affiliates that hold second lien or mortgage pool residual interests, they appear to have been carrying out their loss mitigation duties in ways that delay resolution and thereby maximize the option value of such second lien or residual interests, often at the direct expense of the senior tranche holders. Investors in asset-backed securities need to know that servicing is being performed in a way that maximizes the present value of the entire collateral pool without regard to such conflicts, and this can only be done if fiduciary duties flow directly from servicers that are sufficiently kept away from such competing economic interests.

Servicers, securities administrators and trustees must also establish and enforce uniform accounting policies and procedures for loan restructurings. Since the existing securitization contracts did not contemplate the scope and economic impact of the modifications being implemented under today's environment, it is imperative that securitization accounting in the future reflects the actual economic impact of the modified cash flows associated with the restructuring. Where loan modifications involve principal forbearance, there must be recognition of economic losses that affect how cash flows are allocated within securitizations.

7. **Just as the Trust Indenture Act of 1939 requires the appointment of a suitably independent and qualified trustee to act for the benefit of holders of corporate debt securities, model securitization agreements must contain substantive provisions to protect asset-backed security holders**. Right now, trustees of collateral pools play a largely passive role and bear little if any accountability to the holders of securities which they have agreed – and are being compensated – to serve. In practice they do not supervise the servicers of collateral pools, who are often affiliated with the loan originators and therefore have strong incentives not to enforce representation and warranty claims on behalf of investors. Trustees have no practical means of monitoring or reacting to servicer performance, and no incentive to do so.

If one considers that the trustee of a securitization is like the board of directors of a company and the servicer of a collateral pool is functionally like the management, then it must be stated that holders of asset-backed securities are not given the protective rights, relative to those expected to serve them, that shareholders are provided. Securitization legal structures may utilize trustees and holders of asset-backed securities may have their rights shaped by contracts, but these holders are collectively the equity of the trust and they are owed fiduciary duties which must be respected. At least shareholders have the right to find out who their fellow security holders are, the right to an annual meeting, and the right to remove and elect new directors. Holders of asset-backed securities have none of these rights.

Given servicer incentives and conflicts of interest, the only effective way to effectively enforce deal representations and warranties back to the originator or sponsor is to give investors the ability to re-underwrite the loans as per initial collateral guidelines. Current private-market ABS legal structures seriously limit investors' access to data and ability to require put-backs of bad collateral by onerous minimum ownership hurdles and legal procedures. Legal rights to the integrity of pool collateral without a practical means of enforcement are meaningless in practice, both as a deterrent to originators' knowingly dumping bad assets into ABS pools and as a remedy to investors harmed by such practices.

8. **Asset-backed securities should be explicitly made subject to private right of action provisions of anti-fraud statutes in securities law and to appropriate Sarbanes-Oxley disclosures and controls.** Just as these legal provisions extend to equity and debt securities and help to support investor confidence that they are being treated fairly by issuers, they should similarly extend to asset-backed securities.

9. **Certain asset-backed securities could be simplified and standardized so as to encourage increased trading in the secondary market on venues, such as exchanges, where trading prices are more visible to investors and regulators.** This could result in better price discovery, additional market transparency, additional liquidity and reduced bid/ask spreads. In the interim, investors should be strongly encouraged to buy only those financial instruments which they have an understanding of and are able to analyze completely, including the instruments' current market value. All dealers should be required to disclose historical trade prices on these simplified and standardized asset-backed and structured finance securities daily.

10. **Ratings agencies need to use loan-level data in their initial ratings and to update their assumptions and ratings as market conditions evolve and collateral performance is reported.** The poor record of recently issued asset-backed securities, in light of high initial ratings which were infrequently if at all updated as collateral performance came in, shows that we need fundamental change in the ratings process.

Rating agencies should have to base initial ratings on loan-level data with publicly disclosed economic and collateral performance assumptions including a life-loss curve. As time goes on, they should be required to update their models periodically with updated economic assumptions and new monthly remittance data from servicers. There should be regular secondary market re-ratings, frequent and timely enough to be of real use to investors. Each

NRSRO should have an independent office of a chief statistician that would archive and update ratings models firm-wide, and should be paid based on the accuracy of their ratings as collateral performance is reported. Rating agencies should have their liability exemptions carved back, should have minimum industry standards for analyst professional training in structured finance, and should prohibit revolving-door employee moves to issuers and underwriters. (Of course analysts should be able to join investor firms after leaving the rating agencies as there is not the same conflict of interest as with issuers and underwriters.)

We should create financial and reputation-based incentives for rating agencies to utilize a regular loan-level and cash flow approach to re-rating securities on a regular and frequent basis and their income should be specifically tied to the performance of the rated securities over the life of the issue.

Conclusion

Securitization has shifted significant funding for many asset classes away from bank balance sheets and into the hands of capital markets participants. With appropriate standards and rights for the holders of asset-backed securities, securitization would more efficiently fund markets, result in less volatility, and produce a better convergence between the pricing and value of assets in support of economic activity. This is the reason that we must now restart the securitization markets. If these markets are not functioning as an alternative to portfolio lending where economically less expensive, then there is no way to finance an economy that has previously been funded by global capital flows.

Given the problems in the securitization market that have been exposed by the financial crisis, if the fundamental market restructuring steps taken above are not taken then it will be difficult if not impossible for capital market investors to return to funding economic activity to the degree that they did previously.